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TWO THOUSAND TWELVE

UNITED STATES ARMY



# BUILDING ON A FOUNDATION OF **STRENGTH**

Fiscal Year 2012 United States Army Annual Financial Report

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# BUILDING ON A FOUNDATION OF STRENGTH

Fiscal Year 2012 United States Army Annual Financial Report



**On the Cover (From Left to Right, Top to Bottom):** Combat engineers prepare to maneuver sections of an improved ribbon bridge in a bridge erection boat / Two U.S. Army Soldiers breach a wire obstacle during a situational training exercise. (U.S. Army Photo by Visual Information Specialist Gertrud Zach, Released) / A Soldier performs a foot march during a training event. (U.S. Army photo by Visual Information Specialist Gertrud Zach/Released) / A U.S. Army AH-64 Apache attack helicopter prepares to depart Bagram Air Field, Afghanistan. (U.S. Air Force photo, Tech. Sgt. Matt Hecht) / A paratrooper provides overwatch security to fellow paratroopers. (U.S. Army photo by Sgt. Michael J. MacLeod) / A combat engineer places a Bangalore torpedo during a platoon concertina wire breach. (U.S. Army photo by Sgt. Heather Denby) / An Afghan company executive officer suggests a route of approach into a village to a platoon leader. (U.S. Army photo by Sgt. Michael J. MacLeod) / A U.S. Army sergeant goes across the rope bridge at an obstacle course. (U.S. Army photo by Visual Information Specialist Markus Rauchenberger/Released)

\*Unless otherwise noted, all photos on the cover and inside pages are courtesy of the U.S. Army. ([www.army.mil](http://www.army.mil))



TWO THOUSAND TWELVE

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**"Our Army is built on strong bonds of trust. We trust in our Soldiers who make up our high-quality, all-volunteer force. Those Soldiers in turn trust in the Army and their Families to be their champions in providing a foundation of support needed to succeed."**

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— John M. McHugh, Secretary of the Army



During this past year, the Army has confronted simultaneous challenges to reshape our force, address declining budgets, and continue to defend our national security interests. Our Army and its Soldiers—more than a million strong—have met these challenges, defending and serving our nation with courage and distinction. They are devoted to duty, committed to their missions, and sacrifice on our behalf each and every day.

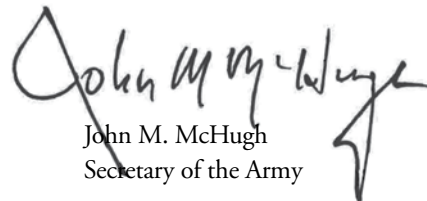
Our Army is built on strong bonds of trust. We trust in our Soldiers who make up our high-quality, all-volunteer force. Those Soldiers in turn trust in the Army and their Families to be their champions in providing a foundation of support needed to succeed. The Army is committed to improving its support systems, from enhancing Wounded Warrior programs to sustaining high-quality housing, child care, and recreation services.

Of course, the Army must have the trust of the American people and confidence in how we use their tax dollars. The Army fiscal year 2012 financial statements are a testament to our strong commitment to accountability and effective management of financial resources. These statements demonstrate our stewardship in how these resources were used to lead, maintain, train, organize, and equip America's Army.

Though our financial resources are declining, we must continue to provide a highly capable force that can preserve the President's strategic options. It is our responsibility to maximize the Army's overall efficiency by identifying and eliminating duplicative or unnecessary programs while still responsibly winding down our commitments abroad and ensuring we can meet emerging threats around the world.

We are moving towards a leaner, more capable and adaptable Army. We will continue to scrutinize budgets as we transition to a smaller yet effective force. We must rebalance force structure and make investment decisions that will shape an Army of 2020 that is prepared for missions across a full range of military operations. This vision focuses on developing adaptive leaders and organizations, modernizing equipment and systems, and revolutionizing training.

I am confident the Army will overcome these challenges and come out stronger. With your continued support and partnership, we will shape the Army not just to come to terms with the constraints of today, but to meet the challenges of tomorrow. We are, and will continue to be, the *Strength of the Nation*.

  
John M. McHugh  
Secretary of the Army

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**"We are building on the momentum achieved through these accomplishments and advancing a culture of accountability across the Army. By implementing efficient and adaptive processes, we are making the Army a more agile and cost-effective organization."**

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– Dr. Mary Sally Matiella, CPA, Assistant Secretary of the Army  
(Financial Management and Comptroller)





The Army has experienced dramatic advances in its business and financial operations in the last three years and more are coming. The end result will be an Army that can produce timely, reliable, and accurate financial information that supports the highest standards of military readiness and accountability.

Changes to the business environment come at a time of great challenge to all of the military services. In addition to the strain of war, we are challenged by the reduction of defense budgets and spending caps established by the Budget Control Act of 2011. These constraints make improved financial operations and strengthened fiscal stewardship top priorities throughout the enterprise.

One of our proudest achievements this last year is completing the deployment of the General Fund Enterprise Business System (GFEBS) in July 2012. The system has more than 52,000 users at more than 200 locations across the globe. GFEBS, now one of the largest enterprise resource planning systems in the world, brings automated processes and controls to the Army's business that result in more timely, reliable, and accurate business and financial information.

In addition, this past fiscal year marked many milestones that demonstrate Army's financial improvement progress. First, in November 2011, an independent public auditor issued a qualified audit opinion on the first of three examinations, we call "mock audits," of business processes related to the Statement of Budgetary Resources (SBR). This is a major achievement and helped us pinpoint areas of improvement and highlighted the consistency of processes across the three installations examined. Second, in August 2012, we initiated the second examination, which covers 10 installations, plus our major service provider, Defense Finance and Accounting Service, as well as an IT audit of GFEBS. Finally, we have begun an audit of three missile programs—the Javelin, Hellfire, and Tube-launched, Optically tracked, Wire-guided (TOW)—to demonstrate our missile property records are accurate and auditable; this represents one of the first major milestones in demonstrating progress toward audit readiness of our assets and progress towards achieving auditability on our complete Financial Statements in 2017.

We are building on the momentum achieved through these accomplishments and advancing a culture of accountability across the Army. By implementing efficient and adaptive processes, we are making the Army a more agile and cost-effective organization. Holding ourselves to the highest standards of accountability in our business operations is essential—we owe it to Congress, the American taxpayers, and our very own Soldiers.

A handwritten signature in black ink that reads "Mary S. Matiella".

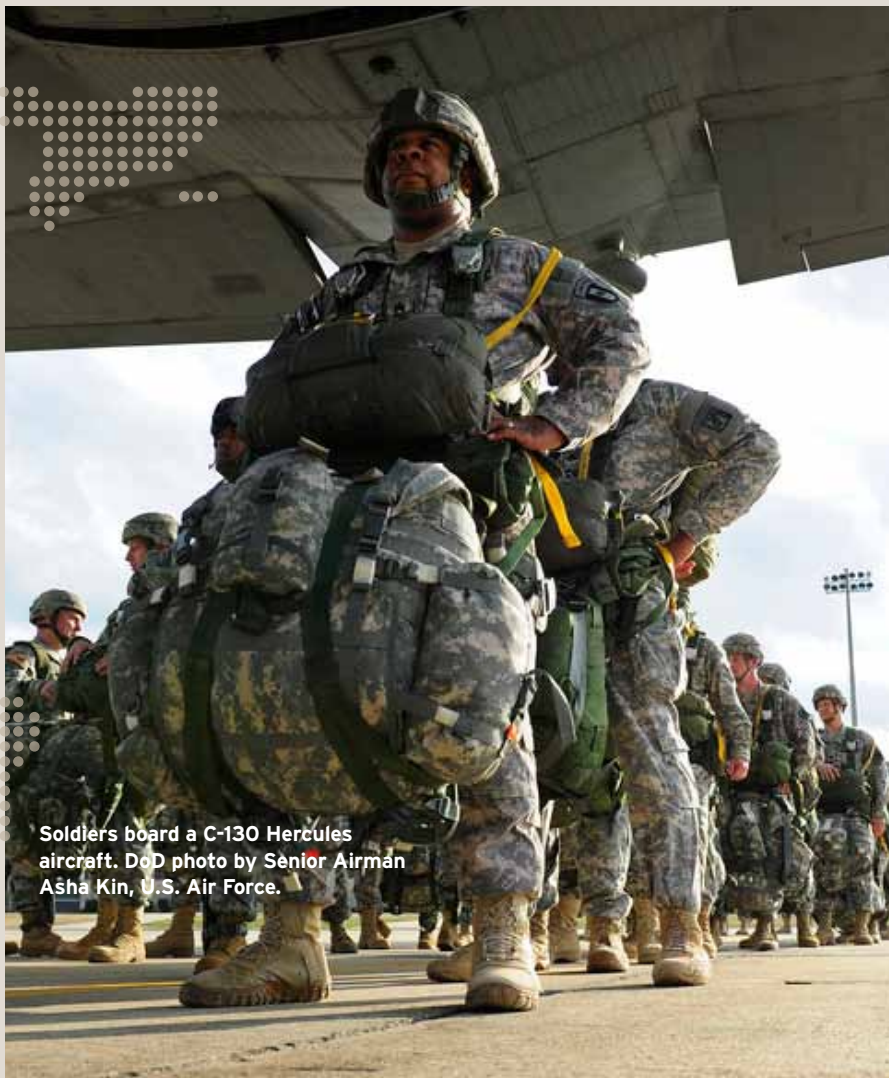
Dr. Mary Sally Matiella, CPA  
Assistant Secretary of the Army  
(Financial Management and Comptroller)



# 2012

**"The strength of our democracy has always rested on the willingness of those who believe in its values and in their will to serve, to give something back to this country, to fight and to sacrifice; above all, to do that in times of crisis."**

— The Honorable Leon E. Panetta (Secretary of Defense)



Soldiers board a C-130 Hercules aircraft. DoD photo by Senior Airman Asha Kin, U.S. Air Force.



Members of a UH-60 Black Hawk helicopter crew come in for a dust landing during an air assault training mission. DoD photo by Sgt. Daniel Schroeder, U.S. Army.



A National Guardsman provides security for fellow members of Kandahar Provincial Reconstruction Team. Photo courtesy of the U.S. Army.

## OVERVIEW

The past decade of conflict has been a period of significant challenge and high operational tempo (OPTEMPO). The Army has emerged as a transformed and highly-capable force that remains the world's preeminent land power. Stress on the force began to ease in Fiscal Year (FY) 2012, when, in December 2011, it concluded combat and stability operations in Iraq. The Army remains focused on accomplishing current missions, with approximately 179,000 Active Component (AC) and Reserve Component (RC) Soldiers<sup>1</sup> deployed or forward-stationed. This includes more than 59,000 Soldiers in Afghanistan who continue to conduct combat operations while transferring security responsibilities to the Afghanistan National Security Forces.

The Army continues to maintain the quality and viability of the all-volunteer force and has met FY 2012 recruiting requirements in all components. The Army is committed to sustaining the optimum levels of support that Soldiers and families deserve by ensuring they receive the right programs and services, at the right times, in the right venues. The Army Family Covenant, now entering its fifth year, represents an overarching commitment to provide quality-of-life programs to Soldiers, and their families, regardless of component or geographic location. The Family Covenant is twofold in purpose: It recognizes the strength and commitment of Soldiers and their families, and, it establishes an enduring partnership with Army Families to enhance their strength, readiness, and resilience.

Warfighting remains the Army's primary mission. To prepare Soldiers, units, and equipment, the Army must maintain a high level of training and readiness. During the past year, it provided trained and ready forces to commanders around the world in

addition to meeting critical homeland defense requirements. In FY 2012, the Army exceeded its ground OPTEMPO goals for the AC and the Army National Guard (ARNG) and exceeded air OPTEMPO goals for the ARNG and the U.S. Army Reserve (USAR). Due to limited dwell times between rotations, the impact of equipment reset requirements, and changes in unit deployment schedules that were not programmed, the AC met 98 percent of its air OPTEMPO goal in FY 2012. The USAR met 89 percent of its ground OPTEMPO goal.

The Army is also committed to providing the best available equipment to deploying Soldiers. The Rapid Fielding Initiative (RFI) continues to enhance warfighting capabilities to address immediate Soldier requirements. A total of 61 brigade combat teams (BCT), 20 combat aviation brigades (CAB), and numerous other deploying units, totaling 230,454 Soldiers, received RFI equipment during FY 2012. In addition, the Army's Rapid Equipping Force (REF) introduced more than 170 different types of equipment (over 38,982 individual items of equipment) to meet the urgent operational requirements of deployed units in FY 2012.

As it enters a period of transition, the Army is applying lessons learned in recent combat operations to prepare for evolving threats. It also continues to rebalance force structure and is making investment decisions to shape an Army that will remain adaptive, innovative, versatile, and ready as part of Joint Force 2020. Over the next five years, the Army will decrease its end strength from peak authorized levels of approximately 570,000 to 490,000 AC Soldiers; 358,000 to 353,500 ARNG Soldiers; and 206,000 to 205,000 USAR Soldiers.

<sup>1</sup> It is Army policy to capitalize the word "Soldiers" when referring to a member of the U.S. Army.

# MISSION AND ORGANIZATION OF THE ARMY

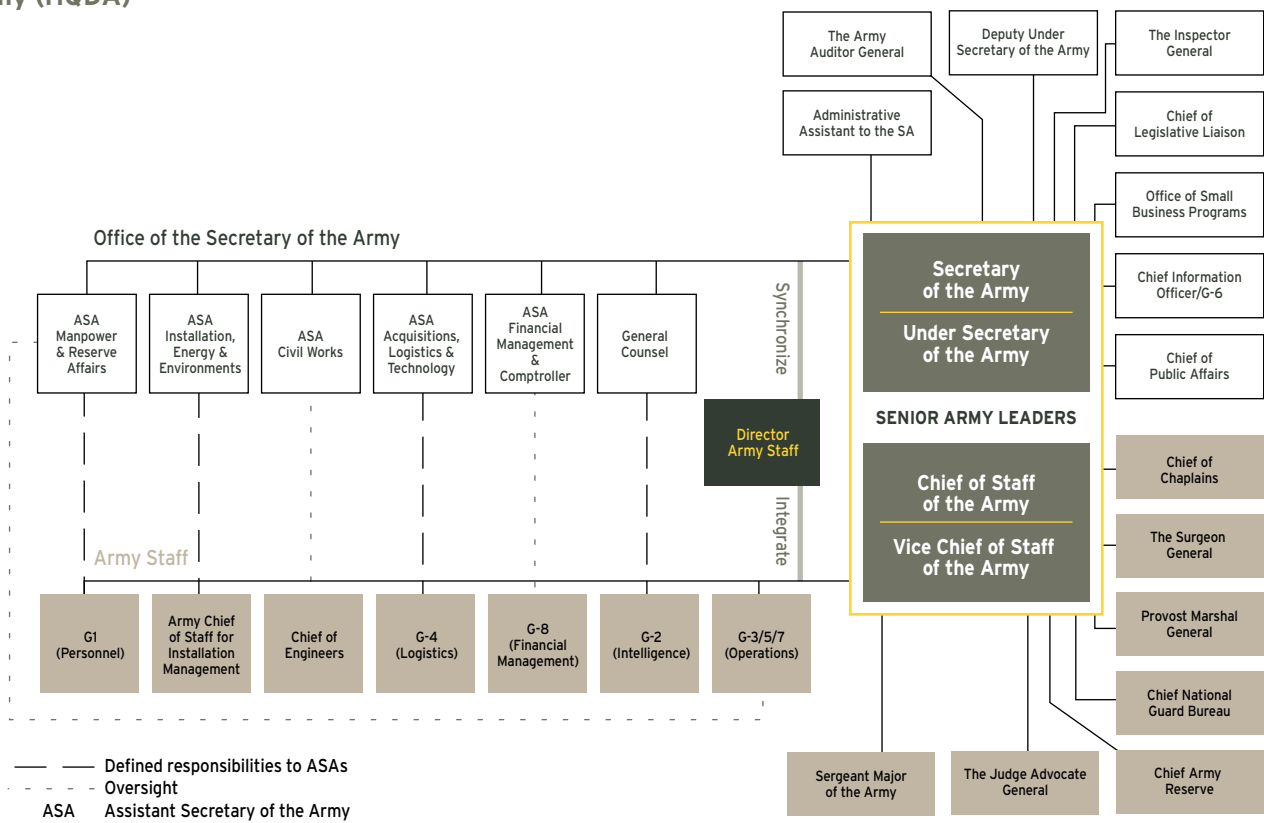
The mission of the United States Army is to fight and win the nation’s wars through prompt and sustained land combat, as part of the joint force. To do this, the Army organizes, equips, and trains Soldiers for rapid, sustained land combat operations; integrates Army capabilities with those of the other armed services; accomplishes all missions assigned by the President, Secretary of Defense, and combatant commanders; and remains ready while preparing for the future.

The Army is organized to support and sustain the mobilization, training, and deployment of its Soldiers anywhere in the world. Headquarters, Department of the Army (HQDA) (Figure 1), under the direction of the Secretary of the Army and the Army Chief of Staff, lead and manage the entire Army. The HQDA Staff is composed of the Office of the Secretary of the Army

(Secretariat) and the Army Staff (ARSTAF). The HQDA Staff supports the Secretary by:

- Developing policies, plans, and programs.
- Establishing and prioritizing requirements.
- Providing resources to organize, man, train, and equip Soldiers to meet the combatant commands’ current and future operational requirements and other needs as defined by the President, the Secretary of Defense, and the Secretary of the Army.

**FIGURE 1. Headquarters, Department of the Army (HQDA)**

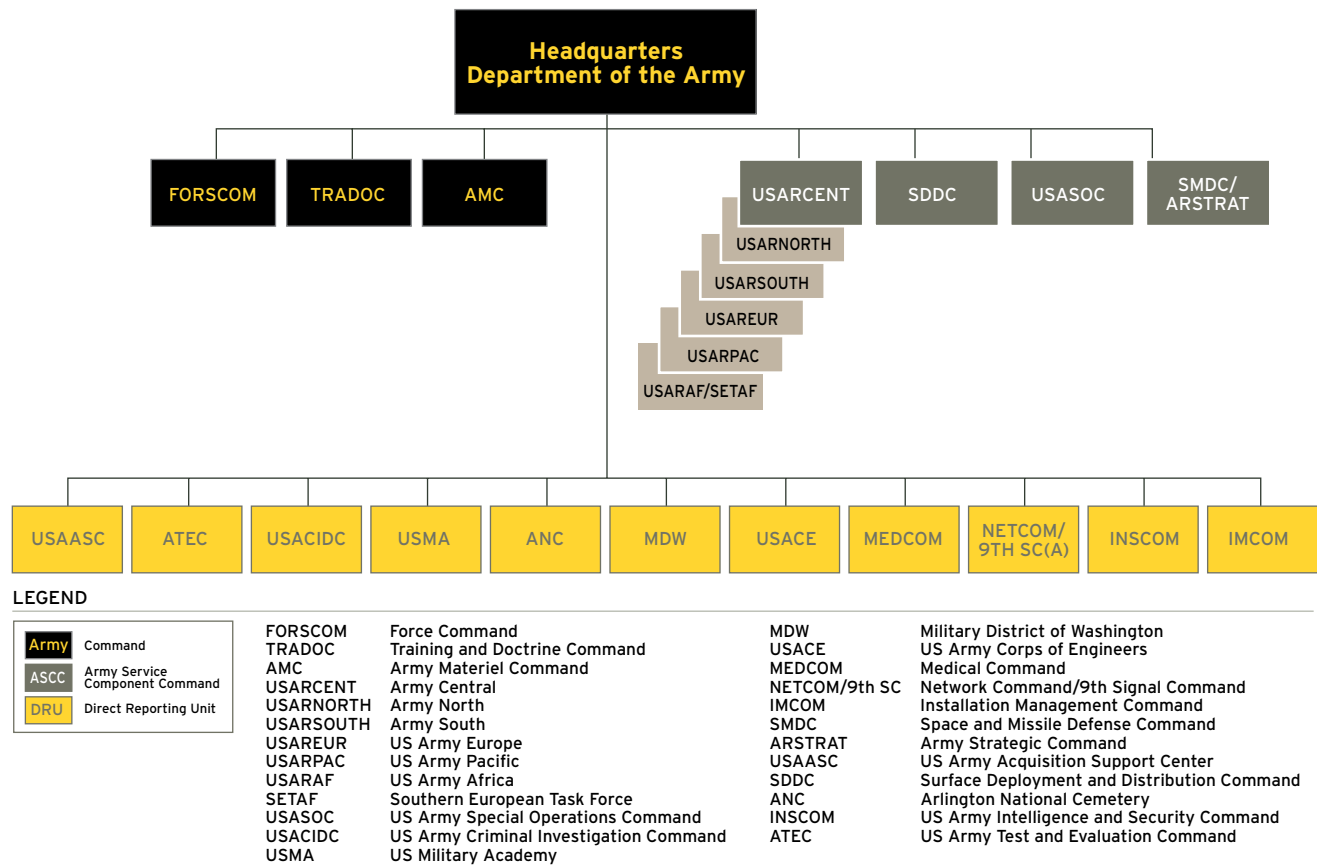


The Army’s command structure (Figure 2) consists of two interdependent elements: the warfighting or operating force, and the generating force. Organizations reporting to HQDA include Army commands, Army service component commands, and direct reporting units.

The operational Army consists of numbered armies, corps, divisions, brigades, and battalions that conduct the full range of global military operations. The institutional Army supports the operational Army by providing the infrastructure necessary to raise, train, equip, deploy, and ensure the readiness of all Army forces.



FIGURE 2. Army Command Structure



The Army's AC consists of full-time Soldiers assigned to the operational and institutional organizations that perform day-to-day Army missions. The RC consists of the ARNG and the USAR. The Congress annually reviews and mandates the number of Soldiers that the Army may maintain.

The ARNG has a dual role. Its first role is that of a state military force to train for, and respond to, domestic emergencies and other missions required by state law. The ARNG can also serve a federal role as part of the operational force, providing trained and ready forces for wartime, national emergencies, and other contingencies. Unless federally-mobilized, ARNG units are commanded by their state executive, usually the governor.

The USAR is the primary federal reserve force of the Army. The USAR provides specialized units and resources to support and sustain the deployment of Army forces around the globe. In addition, it is the primary source for individual Soldiers needed to augment headquarters staff and fill vacancies in the AC.

The Army has been meeting the nation's challenges for over 237 years, and it remains positioned to defend America regardless of future challenges.

## PERFORMANCE GOALS, OBJECTIVES, AND RESULTS

The Army is poised to meet its performance goals by the end of FY 2013. The Army will continue to strengthen the profession of arms and preserve the all-volunteer force. It will build a versatile mix of capabilities, formations, and equipment; and continue efforts to enhance the capabilities of its Soldiers by maintaining a sharp focus on Army Families. In this regard, it is critical that the Army implements a modernization plan that enables it to develop, field, and maintain equipment in a more responsive

and affordable manner. The Army will make fiscally-informed investments, thoroughly reviewing costs, benefits, risks, and potential areas for trade-offs. It will fully align requirements, acquisition, resource, and sustainment processes to ensure they are collectively focused on a common goal. Finally, the Army will develop, field, and sustain the right equipment to provide Soldiers and units the capabilities they need to be successful.



Soldiers part of an expeditionary sustainment command prepare to perform sling load operations. U.S. Army Photo by Army Sgt. Peter J. Berardi.



A Soldier makes the commitment to reenlist. Photo courtesy of the U.S. Army.

Sustain

The Army must maintain the quality and viability of the all-volunteer force, as well as the many capabilities it provides the nation, in order to sustain Soldiers, Families, and Army Civilians<sup>2</sup> in an era of persistent conflict. Sustainment ensures that Soldiers and their families have the quality of life they deserve, leading to improved retention rates.

Manning the Force—Recruiting and Retaining Soldiers

While the recruiting environment is challenging, the Army remains committed to bringing only the very best into its ranks. The Army’s goal is to achieve no less than a 90 percent rate of new recruits with Tier 1 educational credentials, i.e., high school diplomas or above. The Army achieved over 95 percent Tier 1 recruits in FY 2012, down slightly from FY 2011 due to a pilot program that attempts to identify the motivation level of General Equivalency Diploma or alternative credential Tier II applicants. Without the pilot, the Army would have achieved 99.9 percent Tier 1 accessions. The overall attrition rate remained virtually unchanged over the last three years. The static rate and overall quality of recruits are positive signs that the Army is recruiting, training, and retaining a highly-qualified force.

TABLE 1. Quality - Percent Tier 1 Educational Credential Holders (Active Component)<sup>1</sup>

TIER 1	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Goal	90%	90%	90%	90%	90%
Actual	83%	95%	98%	99%	96%

Note 1: Performance Measure. The Army met its recruiting requirements in all components. A weak national economy in FY 2013 is also expected to yield high-quality recruits.

<sup>2</sup> It is Army policy to capitalize the words “Families” and “Civilians” when used in a series with the word “Soldiers.”

**TABLE 2. Accessions**

	FY 2008 Actual	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Goal	FY 2012 Actual
Active Component	80,517	70,045	74,577	64,019	58,000	53,324
Army National Guard	62,397	52,014	57,204	47,206	43,000	39,796
Army Reserve	26,945	23,684	26,795	19,996	16,000	14,195

**TABLE 3. Active Component End Strength Within 2 Percent<sup>1</sup>**

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Goal	529,191	552,400	562,400	569,400	562,000
Congressional Baseline	525,400	532,400	562,400	569,400	562,000
Actual	543,645	553,044	566,045	566,500	551,503
Percent Delta	+3.5%	+3.9%	+0.7%	-0.5%	-1.9%

*Note 1: Performance Measure. The number of Soldiers on active duty at the end of the year; data are as of the end-of-month (EOM), July 2012. Under presidential-declared states of national emergency, end-strength limits may be waived. (End of FY data available in the second week of October.)*

**TABLE 4. Reserve (ARNG and USAR) End Strength Within 2 Percent<sup>1</sup>**

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Goal	556,300	563,200	563,200	563,200	564,200
Actual	557,375	563,688	567,296	567,010	559,610
Percent Delta	+0.2%	+0.1%	+0.7%	+0.7%	-0.1%

*Note 1: Performance Measure. The number of Soldiers in the ARNG and the USAR at the EOM, August 2012.*



A National Guardsman pulls security from his battle position during an escort detail in Afghanistan. Photo courtesy of the U.S. Army.



TABLE 5. Active and Reserve Component Retention<sup>1</sup>

	FY 2008 Actual	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Goal	FY 2012 Actual <sup>2</sup>
Active Component	73,913	68,387	60,000	43,626	61,800	61,800
Army National Guard	29,618	36,672	30,472	39,750	53,077	53,077
Army Reserve	16,523	11,163	10,330	12,934	13,106	13,810

Note 1: Actual retention accomplishments are recorded no later than 18 October 2012.

Note 2: Performance Measure. The number of Soldiers reenlisted during a given FY against published goals. All components achieved their retention mission for FY 2012 as of the end of September 2012. The AC FY 2012 actual includes Soldiers who extended enlistments for deployment through the Deployment Extension Incentive Pay program.

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Due to overseas contingency operations (OCO), several special skills remain in high demand. In FY 2012, the Army continued to offer a Critical Skills Retention and Selective Reenlistment Bonus to attract and retain personnel in specific skills areas, including Special Forces and Military Intelligence. These bonuses, which are vital tools in retaining Soldiers who possess valuable combat experience, have helped the Army to exceed its FY 2012 retention goal. Careful and deliberate adjustments to bonuses, including designation of targeted critical skills, ensured the correct mixture of skilled Soldiers.

Recruiting and retaining Soldiers—confident, adaptive, competent, and able to handle the full complexity of 21st century warfare in a combined, joint, expeditionary environment—is a highly-competitive endeavor. The Army will continue to develop and implement programs to address this challenge.

*Improving the Quality of Life for Soldiers and Their Families*

In order to retain Soldiers, the Army must care for them and their families by providing exceptional programs and services that both meet their needs and support their well-being. The Army is committed to improving the quality of life of AC, ARNG, and USAR Soldiers and their families equal to the quality of their service to the nation. The Army demonstrates this commitment through the Army Family Covenant and the Army Family Action Plan.

The Army Family Covenant supports and sustains the resiliency of an all-volunteer force through strong and vibrant Soldier and family programs, health care, housing, school support, child and youth services, and recreational and quality-of-life opportunities for single Soldiers. The Army has joined forces with communities across the country to inspire support that complements or fills gaps in existing Army programs. These programs provide Soldiers and families of all components with a balanced array of services that meet the unique demands of a military lifestyle. Such services foster life-skill competencies, strengthen coping skills, encourage resiliency instead of dependence, and offer short-term support and assistance when needed.

Other improvements during FY 2012 include:

- Increasing the number of military family life consultants from 112 (FY 2005) to 626.
- Completing 107 child development centers since January 2008 to provide an additional 17,236 child care spaces and significantly reduce waiting lists at 49 installations.

- Maintaining a 97 percent national accreditation rate of Army child development programs.
- Providing over one million hours of respite child care to reduce stress on deployed families.
- Supporting more than 103,000 geographically-dispersed AC and RC children, in 40 states who participated in youth outreach activities, camps, and workshops offered through Operation Military Kids.
- Maintaining Soldier and Family Assistance Centers (SFAC).
- Placing thousands of spouses in jobs through the Army Spouse Employment Program.

### *Warrior Care and Transition*

With the continued maturation of the Army's Warrior Care and Transition Program (WCTP), wounded, ill, and injured Soldiers and their families are receiving the care management and support they need and deserve. The Warrior Transition Command (WTC) was created to ensure focused and effective management across all aspects of the WCTP. In FY 2012, the Army dedicated \$800 million to equip the WCTP with support staff, training, information technology (IT), and to make investments in 20 facilities, 31 SFACs, and 64 administrative headquarters. Staff across the enterprise included all components, and contractors—almost 4,000 squad leaders, platoon sergeants, nurse case managers, and support staffs coordinating care in warrior transition units (WTUs) and community-based WTUs (CBWTU).

With the WTC leading the way, the Army cares for over 21,000 Soldiers and veterans annually. The WTC's Wounded Warrior Program assists and advocates for over 12,000 severely-wounded, ill, and injured Soldiers, veterans, and their families and caregivers. Their wounds, illnesses, and injuries range from loss of hearing or vision, to amputations, burns, paralysis, traumatic brain injury, and post-traumatic stress, or to incurable and fatal diseases. This population is supported by over 200 advocates located at major military treatment facilities, Army installations, Department of Veterans Affairs (VA) medical centers, and in local communities throughout the continental United States, Alaska, Hawaii, Puerto Rico, and Germany. Advocates function as integrated, collaborative members of multidisciplinary healthcare and benefits teams within the WTUs, CBWTUs, and VA. There are over 2,000 wounded warriors, supported at nine CBWTUs, who have been provided the opportunity to heal in their home communities with their families. Approximately 8,050 additional wounded warriors are supported at 29 WTU locations across the nation.



**A Soldier holds the hand of his son upon his return after a year-long deployment to Kosovo. DoD photo by Senior Master Sgt. David H. Lipp. (Released)**

To help each warrior to return either to the force or to veteran status, the Army developed a systematic framework known as the comprehensive transition plan (CTP). The CTP is a six-part process, which includes an individual plan created by the Soldier with the assistance of a dedicated cadre and support personnel. Using a standardized framework, this process enables wounded and ill Soldiers to customize their recovery plans, and empowers them to set and reach their personal goals. In FY 2012, funding helped approximately 50 percent of the wounded warrior population return to duty. Other wounded warriors have successfully transitioned to civilian life to further their educations, or enter the workforce. The program's initial success can be attributed, in part, to an aggressive, non-clinical rehabilitative approach. The funding-supported pillars of this program include activities such as:

- Adaptive reconditioning (active and mental stamina activities).
- Inauguration of the warrior games at the U.S. Paralympic athlete competition.
- Comprehensive Soldier fitness—performance enhancement.
- Resiliency training.
- Programs geared toward the holistic healing and mental and physical fitness of wounded, ill, and injured Soldiers.

### *Improving Soldier and Family Housing*

The Army's commitment, coupled with the Congress' support for housing programs, brings to reality our pledge to provide a quality of life for Soldiers and their families commensurate with their service. In concert with the private sector, the Army continues to bring to bear considerable effort to improve both family housing and the Barracks Modernization Program. The Army's inventory of inadequate family housing has been eliminated at enduring U.S. locations through privatization and the demolition or divestiture of uneconomical and excess units. The Army will move forward to improve or replace family residences worldwide in order to provide adequate housing and to meet Defense Department goals; these improvements are reflected in its property records.

The privatization of homes at 44 installations has been completed on schedule. These 44 installations have an end-state inventory of 85,424 homes. The Residential Communities Initiative program is in the portfolio and asset management phase.

The Army is on track to eliminate inadequate, common area latrines in permanent party, single-Soldier barracks, and to complete the modernization program in the near future. The FY 2013 permanent-party barracks projects—which were deferred or placed on hold to reduce the risk of over-building due to pending stationing decisions—will be addressed in the FY 2015-2019 Program Objective Memorandum (POM). As of FY 2012, the Army has 147,913 adequate spaces funded out of 154,505 spaces required.

The Army's strategic Training Barracks Modernization Program remains on course for completion in FY 2017, with new barracks available for occupancy in FY 2019. The construction goal is to eliminate the deficit of spaces and to complete restoration and modernization of 91,530 soldier spaces during the time potential occupants attend basic training, one-station unit training, or advanced individual training. As of FY 2012, 60,633 spaces have been funded.

The Army executed four unaccompanied personnel housing privatization initiatives for staff sergeants and above at Forts Irwin (CA), Drum (NY), Bragg (NC), and Stewart (GA). Together, these facilities will provide 1,586 one- and two-bedroom apartments in areas that have limited civilian-owned rental properties available.

### **Prepare**

To prepare Soldiers, units, and equipment, the Army must maintain a high level of readiness for the current operational environments, especially in Afghanistan and Iraq, while taking into consideration potential future conflicts. The Army is continually adapting training and materiel to keep pace with an evolving enemy. It remains committed to providing deploying Soldiers with the best available equipment in order to maintain a technological advantage over any enemy soldiers may face.

### *Providing Support for Operational Requirements*

The pace of operations in the new security environment presents a number of significant force management challenges. Due to the Army's global commitments, approximately 179,000 Soldiers are deployed or forward-stationed in nearly 170 countries. As of 20 September 2012, approximately 551,600 personnel were serving in the AC, and approximately 47,600 RC Soldiers were on mobilization orders.

Repeated deployments affect recruiting and retention and have a significant impact on the Army's ability to care for Soldiers and their families. Consequently, it is examining and pursuing numerous initiatives that will reduce force-management risk in meeting today's challenges, and in better positioning Soldiers for the future.



Looking out the side of a UH-60 Black Hawk helicopter in preparation to land and dismount while conducting training for contingency operations. Photo courtesy of the U.S. Army.





A Soldier places a Bangalore torpedo during a platoon concertina wire breach in a local training area after a 12-month deployment in support of Operation Enduring Freedom. U.S. Army photo by Sgt. Heather Denby.

The Army Force Generation (ARFORGEN) process uses a three-stage cycle (Reset, Train/Ready and Available) and a modular approach to unit structure to create a sustainable process employing a rotational, more predictable plan for deployments with the ability to surge combat power when needed for major operations. When fully operational, ARFORGEN will enable the Army to effectively and efficiently schedule fully-ready units for deployment. In turn, this will:

- Reduce uncertainty for Soldiers, families, and the local communities that support installations.
- Improve the availability of forces for combatant commanders.
- Generate a continuous number of available BCTs, augmented by all required supporting organizations (given appropriate mobilization authority).

- Enable the Army to surge additional BCTs augmented by all required supporting organizations (given appropriate mobilization authority).

### *Training Soldiers*

Initial entry training develops warfighting capability through training in individual warrior tasks and battle drills. To ensure tasks remain relevant to the operating environment, the Army reviews and updates these tasks and drills every two years.

The Army continues to augment its ability to conduct irregular warfare through several multi-functional courses. For example, some courses build on language and cultural competencies while others improve Soldiers' and civilians' knowledge of, and capabilities in, electronic warfare, red teaming (opposing forces), counterterrorism, weapons of mass destruction, civil affairs, information operations, counter-explosive hazards, and operational law.

**TABLE 6. Individual Training<sup>1</sup>**

	Initial Military Training						
	Basic Combat Training	One-Station Unit Training	Advanced Individual Training	Basic Officer Leadership Course	Officer Candidate School	Warrant Officer Entry Course	Initial Entry Rotary Wing
2010 Trained (actual)	75,922	32,126	105,050	18,977	2,306	2,273	1,132
2011 Trained (actual) <sup>2</sup>	73,830	29,583	91,497	17,212	1,424	2,225	1,260
2012 Trained (interim) <sup>2</sup>	49,229	17,419	58,286	11,302	852	1,562	649

*Note 1: This data represents active Army, ARNG, and USAR students graduating from AC schools. All data is based on start date, i.e., if a class started in FY 2011 and graduated in FY 2012, it is counted in the FY 2011 data. Example: Soldiers who attended the basic combat training class that started in August 2010 (FY 2011), and who graduated in November 2011 (FY 2012), are not included above.*

*Note 2: The actual trained data for 2011 and the interim trained data for 2012 are as of 17 September 2012.*

### *Training Units*

In FY 2012, the Army provided trained and ready Soldiers to commanders around the globe in addition to meeting critical homeland defense missions. To make certain Soldiers were combat ready in FY 2012, they engaged in a balanced mix of live, virtual, and constructive training. The AC and RC executed a focused and demanding ground and air training plan, which included actual miles driven and hours flown as well as virtual miles driven and hours flown through the use of simulators. In FY 2012, home-station training miles and hours executed were affected by limited dwell times between rotations, equipment reset requirements, and changes in unit deployment schedules into theaters that were not programmed.

**TABLE 7. Ground and Air Operational Tempo (OPTEMPO) <sup>1, 2</sup>**

	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Goal <sup>3</sup>	FY 2012 Actual
AC Ground OPTEMPO (Mileage)	605.0	427.0	386.0	635.0	1,080.0
AC Air OPTEMPO (Flight Hours)	10.0	9.9	11.4	10.4	10.2
ARNG Ground OPTEMPO (Mileage)	119.0	123.0	108.0	636.0	707.0
ARNG Air OPTEMPO (Flight Hours)	9.4	9.1	8.8	5.5	8.0
USAR Ground OPTEMPO (Mileage)	146.0	132.0	106.0	1,139.0	1,011.0
USAR Air OPTEMPO (Flight Hours)	5.5	5.1	7.3	4.6	5.9

*Note 1: In FY 2012 tank miles were replaced with full spectrum training miles, which is a composite training mile and includes M1, M2, M3, UA-HMMWV and STRYKER variants for AC and ARNG. The USAR includes MTVs and PLS support vehicles.*

*Note 2: FY 2009 through FY 2012 reflects home-station execution only.*

*Note 3: FY 2012 goal is base only funding; execution includes both base and OCO. FY 2012 amounts are estimates based on execution as of September 2012.*

### *Training Support Systems*

The Army's Training Support System (TSS) enables training at home stations, combat training centers (CTC), and institutions by creating realistic conditions that reflect the operational environment. The TSS provides and operates training support products, services, and facilities in the form of critical training enablers, such as ranges and targets; live-virtual-constructive and gaming training aids, devices, simulators, and simulations (TADSS); instrumentation systems; training facilities; maintenance support of TADSS; and training support operations and management.

As a result of Army Training Summit III held in FY 2012, the Army has identified capabilities needed to adapt TSS to support ARFORGEN training requirements and lessons learned from current operations. At home stations, training must support Soldiers, leaders, and units training for decisive action. Ranges are being modernized to integrate digital systems that enable squads and platoons to train as they fight, as well as to provide commanders and leaders with objective data to assess their units' performance and training levels. New TSS capabilities are being fielded to support requirements driven by the Army Campaign Plan. A persistent live, virtual, and constructive integrated training environment will be implemented at selected home stations. This architecture links Home Station Instrumentation Training Systems in live training areas to mission training complexes (MTC), which house constructive simulations and gaming to virtual TADSS.



Moving through an obstacle during USAREUR Expert Field Medical Badge training. U.S. Army photo by Visual Information Specialist Gertrud Zach. (Released)



Students master rappelling from a helicopter during training. U.S. Army photo by Sgt. Richard Wrigley.

The Army is also modernizing the MTCs and training simulations to upgrade leader and battle-staff training and mission-rehearsal capabilities for deploying units. The MTCs give units the ability to train and to sustain critical individual, operator, and battle-staff skills on digital command, control, communications, intelligence, and surveillance and reconnaissance systems. The MTCs also network with other installations and simulations to support joint training exercises. The MTC serves as the hub for an installation's live, virtual, constructive, and integrated-training environment.

Army TSS—including, manpower and operations support required to maintain and operate TADSS—must continue to keep pace with equipment modernization and Army transformation. This will ensure that training supports current operations, addresses ARFORGEN training and readiness requirements, and enables training for full spectrum operations.

### *Adapting Training*

In FY 2012, in spite of deployment demands, the Army conducted 24 of 24 planned rotations at the maneuver CTCs, 36 exercises with the Mission Command Training Program, and 30 mission command seminars. The CTCs provide realistic joint and combined-arms training that approximates actual combat consistent with Army and joint doctrine. The CTCs are at the core of the Army's collective training strategy and have dedicated resources beyond those available at home-station training sites. Training is specifically tailored to prepare units for in-theater conditions as well as to provide a free-thinking-enemy-and-lessons-learned feedback through a professional staff of observer controllers.

While the CTCs do retain the capability for major combat operations-oriented unit training—needed for other potential theaters of war and new modular brigades—the current focus is counter-insurgency operations and lessons learned from combat in Afghanistan and Iraq. The training environment emphasizes rapid change and adaptation to current activities while using improved facilities on the battlefield, and realistic scenarios. As mission requirements are reduced in Afghanistan, the CTCs have started to conduct decisive action rotations that will better prepare the Army's formations for a wider range of contingencies.

The BCTs that are not scheduled to deploy to theater conduct a decisive action rotation. While home-station training focuses on battalion staff and company-level collective training proficiency, the CTCs have the unique capability to train brigade-level and above staffs and to develop battalion-level and above collective tasks. The complex, event-driven scenarios challenge the BCTs to execute multiple, simultaneous missions that include integrated enablers from the Army and the joint community.

### *Growing Adaptive Leaders*

The Army has developed, and will continue to develop, leaders who have proven themselves competent, confident, and agile at every level, and in every cohort and component, in order to meet the current and future challenges. Army leaders have performed magnificently and resiliently in two wars and under a harsh operations tempo, resulting in a rich body of knowledge throughout the Army. The current operational environment proves that leaders must possess skills beyond those of pure tactical warfighting. It demands skills in such disciplines as irregular warfare, information operations, negotiation, cultural awareness, stability and reconstruction operations, as well as foreign language proficiency—and all without losing a warfighting focus.



Due to the current high operational demand, many Army leaders are unable to attend professional military education (PME) at the optimal time in their career. As a result, the Army has a large backlog at nearly all educational levels in both the AC and RC. To slow the growth of the backlog, the Army employed mobile training teams for Noncommissioned Officer Education System courses and increased the use of distributed learning to conduct PME within the constraints of ARFORGEN. As mission requirements change, the Army expects an increasing number of leaders will be available to attend PME, which, in turn, will reduce the current backlog.

**TABLE 8. Professional Development (AC Schools Only)<sup>1</sup>**

	Warrior Leader Course	Advanced Leader Course	Senior Leader Course	Intermediate Level Education Resident (ILE), Common Core <sup>2</sup>	Senior Service College (SSC) Resident & Distance Learning
2010 Trained (actual)	30,190	12,717	9,893	1,124/912	198/326
2011 Trained (actual) <sup>3</sup>	29,022	18,930	10,795	1,071/614	210/338
2012 Trained (interim) <sup>3</sup>	49,229	17,419	58,286	0/634	509/330

*Note 1: This data represents active Army, ARNG, and USAR students graduating from active component schools. All data is based on start date (i.e., if a class starts in FY 2011 and graduates in FY 2012, it is counted as FY 2011 data).*

*Note 2: The 2012 resident ILE classes do not graduate (1,201 inputs) until December 2012 and June 2013.*

*Note 3: Actual 2011 trained data and interim 2012 trained data are as of 17 September 2012.*

The Army is keenly aware of the valuable contributions made by its civilian corps in supporting the National Military Strategy. Here, too, it must provide training, education, and operational experiences that develop and improve the leadership competencies which, collectively, enhance this cadre's ability to support Soldiers, the Army, and the nation. To advance this goal, the Army revamped its Civilian Leader Development Program in FY 2012 to better align it with the Military Leader Development Program. Specifically, the Civilian Education System (CES) meets the Secretary of the Army's mandate that the leaders of tomorrow be adaptable and multi-skilled. This mandate demands a centralized education, training, and development program in which to develop civilian leaders who—in both operational and institutional capacities, and in evolving environments—can meet and succeed in their missions.

**TABLE 9. Civilian Professional Development**

	Army War College	Industrial College of the Armed Forces	Civilian Education System
2012 Inputs	14	7	56,344

The CES uses leadership competencies derived from those set by the Department of Defense (DoD) civilian leader development framework and those identified by the Center for Army Leadership. The CES courses support and promote career path requirements, professional development, and life-long learning and self-development. Section 1113 of the 2010 National Defense Authorization Act (NDAA) and the Federal Supervisory Training Act outline specific requirements for the development of a mandatory supervisor training course for all DoD supervisors, both civilian and military. In point, supervisor training must include the use of new NDAA authorities, instruction on prohibited personnel practices, and mentoring of new supervisors. First-time supervisors, who are in the job less than two years, are required to complete training no later than one year from the date on which they are appointed to a supervisory position.

The Army has revised its Supervisor Development Course to meet the NDAA requirements. Training for all supervisors of civilian employees promotes the development of world-class leaders and provides opportunities for new managers and supervisors to interact, share experiences, and learn from each other. Supervisor training develops a diverse cadre of leaders capable of managing across the military, ensuring the continuity of the leadership and supervisory pipeline, and promoting the Army's vision for competency-based development across the leadership continuum.

In direct support of the Secretary of the Army's initiative to transform the Army civilian workforce, the Civilian Training and Student Account (CTSA) was established for Army-funded civilians attending an Army SSC, i.e., the Army War College and the Industrial College of the Armed Forces. The account mirrors the Military Trainees, Transients, Holdees, and Students account by reassigning SSC participants to an HQDA-centralized operational table of distribution and allowances. By assigning SSC participants to the CTSA, the losing command can immediately backfill against the position and mitigate any disruption to the organizational mission.

Based on its FY 2011 success, the Army continued using the CTSA in FY 2012, and subsequently placed graduates in enterprise positions most needed by the Army. Other recent initiatives will be developed and implemented to ensure a robust, accessible training program for all Army civilians. These initiatives include, but are not limited to, the following:

- An Army-wide civilian training management system.
- Leader competency-based training in conjunction with the Army competency management system.
- Fellowships and experience-broadening interagency, international, and multinational assignments.
- Increased outreach and communication to the Army civilian corps with the goal of increasing CES participation.
- NDAA-directed supervisory training.

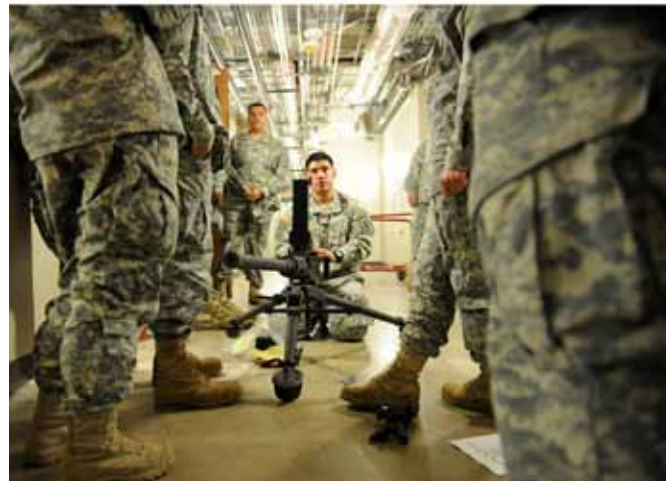
Improvements to the CES, coupled with implementation of transformative initiatives, will create a progressive human resources management framework that puts a premium on employee development performance and potential.

#### ***Acquisition and Cross Servicing Agreements (ACSA) in the U.S. Central Command (CENTCOM) Area of Responsibility (AOR)***

There is concern that the military services are not fully invested in, or often unaware of, the ACSA process within the CENTCOM AOR as CENTCOM executes its authorities to

equip coalition partners with supplies and materiel. The Office of the Deputy Chief of Staff (ODCS), G-3/5/7, requested that the U. S. Army Audit Agency (USAAA) audit the ACSA process to (1) determine if Army organizations are fully aware of all transactions attendant to issuing ammunition to coalition forces, and (2) look at existing controls to determine their adequacy. The ODCS, G-4, established itself as the lead agency for this audit as it is heavily involved in the ACSA ammunitions process.

During the audit's first phase, the USAAA determined that Army organizations within the chain were not fully aware of the scope and breadth of transactions conducted by Army elements, Afghanistan and United States Forces – Iraq (USF-I). The USAAA also determined that organizations were unaware that units were transferring ammunition under the Office of the Secretary of Defense (OSD) Lift and Sustain Program. There is no implementing guidance below the Joint Chiefs of Staff level for ACSAs, nor is there guidance below the OSD level for the ACSA and Lift and Sustain Program. Although ACSAs are negotiated at the combatant commander level, they are executed at the service component level.



**An Infantryman instructs Soldiers on proper use, handling of the M2 .50 caliber machine gun during sergeants time training. Photo courtesy of the U.S. Army.**





A CH-47 Chinook crew chief looks over cargo paperwork for the next load of supplies at the next forward operating base in Afghanistan. Photo courtesy of the U.S. Army.

The ODCS, G-4, established a HQDA Directive, Army Directive 2012-12, *Interim Army Acquisition and Cross-Servicing Agreements, Lift and Sustain, and Foreign Assistance Act Authorities*, which provides consistent guidance to assist Army service component commands in ACSA execution. The directive was signed by the Secretary of the Army on 30 April 2012, with the goal of providing better accountability of all DoD materiel and services provided to other nations.

The RFI enhances warfighting capabilities through modernized technology in addressing the immediate requirements of Soldiers. In the ARFORGEN operating cycle, a total of 61 BCTs, 20 CABs, and numerous other OCO-deploying units—comprising 230,454 Soldiers—were fielded RFI equipment during FY 2012.

The U.S. Army REF harnesses current and emerging technologies to provide immediate response to urgent equipment and materiel requirements of U.S. Army forces fielded globally. The REF's priority is at the deployed brigade and BCT levels, and focuses on commercial off-the-shelf and government off-the-shelf solutions in order to maximize responsiveness and minimize risk. The REF maintains forward-deployed teams that interact with units to identify, equip, and evaluate their requirements and capability shortfalls. In FY 2012 alone, the REF introduced over 171 different types of equipment and provided more than 38,982 individual equipment items to deployed Soldiers and units. The REF is on track to introduce 179 different types of equipment



Soldiers conduct sling-load operations during an evaluation designed to integrate and mature the Army's tactical network. U.S. Army Photo by Spc. Jeanita C. Pisachubbe.

and provide more than 40,151 individual equipment items to deployed Soldiers during FY 2012.

The Army continues to invest in the ARNG and USAR to enhance their mission capabilities and to ready forces entering the ARFORGEN cycle for deployment and homeland defense missions. The fleet age of trucks, combat vehicles, communications systems, and Soldier weapon systems continues to decline as new equipment is fielded to the RC. The ARNG and USAR forces preparing to deploy are accompanied by the very best modernized equipment, eliminating the disparity between the AC and RC, thereby achieving a critical goal in the effort to create strategic depth and operationalize the RC.

## Reset

The Army leverages all available resources—new production, reset, and equipment redistribution, and cross-leveling to meet deployed and deploying unit equipment requirements. Modularity enables smoother transitions between units based on similar designs and equipment requirements. The goal is to ensure Soldiers have the necessary equipment to effectively train and prepare for their next mission by (1) equipping AC units to an S3, operations and training, level by return from operations plus 180 days (up to 270 days for reset aircraft), and (2) equipping RC units to the S3 level by return plus 365 days. With FY 2012 supplemental appropriations support, the Army purchased equipment to fill critical shortages in support



of combat operations and restored equipment to a *ready-to-fight* condition for resetting units. Each year, the Army grows closer to a fully-equipped force by working diligently to fill pre-existing equipment shortages required to close strategic capability gaps while transforming BCTs and support units into a modern, strategically-responsive ground force.

### ***Modification Management Information System-Safety of Use Compliance Reporting***

Army regulations state that AC and RC commands and direct reporting units are to report compliance to the applicable life cycle management command in accordance with the time lines set out in the safety of use (SOU) message. Commands are to report compliance via traditional mail or e-mail to program or item managers. The previously-used reporting process made compliance tracking difficult and the effectiveness of SOU risk mitigation efforts was unknown.

The Army led a Lean Six Sigma (LSS) project in FY 2012 to improve SOU compliance. Team members of the core group consisted of Army Materiel Command, Aviation and Missile Command, Tank and Automotive Command, Communications Electronics Command, Forces Command, and Training and Doctrine Command. The team analyzed the current compliance process and determined that the existing process was insufficient for reporting and tracking compliance.

The current Army system for tracking modification work orders within the Materiel Management Information System (MMIS) was determined the right platform to improve SOU reporting and compliance. The MMIS allows the Soldier to implement corrective actions within a system with which he or she is familiar and using on a regular basis. This fact, coupled with MMIS accessibility increases SOU compliance and risk mitigation; in addition, by utilizing the established MMIS platform, programming expenses are minimized and the training requirement is nominal.

A significant MMIS benefit is process standardization from the initial reporting of actions to subsequent recording of compliance results. Its availability spans senior leadership levels to the junior Soldier executing the SOU solution. Every subscriber to the MMIS has the ability to track SOU distribution and message compliance to ensure the risk mitigation measures employed. Effective 1 October 2011, MMIS became the Army's compliance tool for all ground safety and maintenance messages. The Army will continue to monitor SOU compliance.

### ***Drawdown in Iraq***

The drawdown in Iraq was the largest logistics operation since World War II. While supporting the warfighter, the Army

simultaneously executed the final phase of the withdrawal and redistribution of equipment from Iraq.

The Army met the 31 December 2011 presidential mandate in accordance with the security agreement to withdraw all forces from Iraq and complete the transition to the Department of State (DOS)-led United States Mission-Iraq. The Army redistributed equipment from Iraq to satisfy a variety of requirements, including (1) supported operational needs for U.S. forces in Afghanistan; (2) filled equipment shortages to rebalance the Army; (3) equipped coalition partners with transferred and loaned equipment to enhance their warfighting capabilities; and, (4) supported state and local government needs in the United States.

In addition to retrograding equipment from Iraq, the Army also redistributed equipment within Iraq to meet three critical missions:

- Enable Iraqi Security Forces (ISF) to attain minimum essential capability.
- Support the transition of responsibility to the DOS with required resources and capabilities as they assumed the mission in Iraq after United States Forces-Iraq (USF-I) departed.
- Support the Office of Security Cooperation-Iraq (OSC-I) with required equipment to allow them to continue to advise the ISF and assist with foreign military sales transactions.

The Army transferred equipment to the Government of Iraq (GoI) under the provisions of three congressional authorities, outlined below:

- Excess Defense Articles (Section 516 of the Foreign Assistance Act of 1961 (22 USC 2321j)): 17,936 pieces of equipment were transferred to the GoI, to include helmets and body armor, 5-ton cargo trucks, and older model M16A2 rifles. Equipment was excess to Army requirements.
- Non-Excess Materiel (Section 1234 of the FY 2010 National Defense Authorization Act): 810 pieces of Army non-excess equipment were transferred to the GoI, including M1114 up-armored high-mobility, multipurpose-wheeled vehicles (HMMWV); .50 caliber machine guns; medical sets; 40-ton low-bed trailers; maintenance contact trucks; communication equipment; and palletized loading system flat racks. Equipment supported building capabilities for the ISF.

- Foreign Excess Personal Property (FEPP) (Federal Property and Administrative Services Act of 1949, as amended (40 USC 701-704)): approximately 4.8 million pieces of equipment were transferred under FEPP authorities. Equipment included commercial generators, containerized housing units, light sets, and barrier material for force protection. The majority of the equipment was essential to operating a base.

In total, the Army withdrew approximately 3.4 million pieces of equipment from Iraq, closed or transferred 505 bases to the GoI, closed 22 supply support activities, and transferred 11 bases to the DOS and OSC-I.

### *Enhancing Logistics Readiness*

The Army is implementing a Single Army Logistics Enterprise as its overarching logistics, business, and information technology framework. It is projected to provide department-wide efficiency gains of interoperability, traceability, accountability, auditability, and transparency. Army logistics is making steady progress in fielding enterprise resource planning solutions through the Logistics Modernization Program (LMP) and Global Combat Support System-Army (GCSS-Army). The following are key FY 2012 accomplishments:

Over the last year, the LMP continued to support AMC-deployed sites and plan for future requirements. In November 2011, LMP officially entered the sustainment phase of the of the acquisition life cycle. A follow-on contract was awarded in December 2011, which allowed the Army to continue to enhance the LMP and provide additional capabilities throughout AMC.

At the installation and tactical level, GCSS-Army was successfully fielded to the 2nd Brigade, 1st Armored Division (2/1 AD) at Fort Bliss (TX). In December 2011, the U.S. Army Test and Evaluation Command reported the system effective, suitable, and survivable with limitations, based on the initial operational test and evaluation conducted at the 2/1 AD in October 2011. The achievement of milestone “C” approval and the recommended approval for deployment positions the program for full fielding in FY 2013.

On the depot maintenance front, as of 31 July 2012, more than 95,000 items have been repaired at depot-level facilities. These items include more than 670 tracked vehicles, e.g., Bradley fighting vehicles; more than 2,400 tactical-wheeled vehicles, e.g., HMMWVs and medium- and heavy-tactical vehicles; and more than 18,800 individual and crew-served weapons, e.g., rifles, pistols, and machine guns. Meanwhile, the Army’s special repair teams brought additional depot-level expertise to the field, completing repairs to over 486,000 items, including small arms, night-vision devices, and communications electronics as well as chemical and biological gear. In addition, the Aviation Special Technical Inspection and Repair Program restored more than 315 fixed- and rotary-wing aircraft to combat capability.

## **Transform**

To transform, the Army must continuously improve its ability to meet combatant commander needs in a changing 21st century security environment. Transformation is a holistic effort to adapt how the Army fights; trains; modernizes; develops leaders; bases its forces; and supports Soldiers, Families, and Civilians. Transformation is a journey, not a destination.

### *Growing and Modularizing the Army*

The transition to a BCT-focused organization was the right decision to confront today’s fluid counter-insurgency threats as well as scenarios the Army is likely to face in the years ahead. The evolving nature of conflict—with diverse state and non-state actors employing hybrid and asymmetric approaches to warfighting—will continue to necessitate the range of capabilities inherent in modular BCTs.

The Army’s employment of modular formations and their reset following sustained combat operations helps manage the impact of high operational demand. As America’s dominant and decisive force, the Army remains committed to securing U.S. interests across the full range of operations—from aiding civil authorities and citizens at home, to combating insurgents abroad. The Army continues to execute its most comprehensive transformation since World War II, while simultaneously conducting combat operations with approximately 179,000 deployed Soldiers. The 21st century Army is meeting the challenges of a new security environment characterized by persistent conflict and adaptive enemies in complex environments. The Army continues to make progress across a range of transformative areas, including its Modular Force Initiative (MFI), Army equipment modernization, reset of units returning from combat operations, and the reconstitution of Army prepositioned stocks.

The results of the Army’s assessment of modular force capabilities—including lessons learned from experiences with existing modular units—have driven several modifications. These modifications have reinforced the success of the modular concept and have necessitated only minor alterations to the modular design of these units. A direct result of the lessons learned over the last ten years has been an appreciation for the need to increase following modular capabilities: medical specialists, electronic warfare specialists, company intelligence support teams, and unit supply specialists.

In addition to modular design changes, lessons learned have given rise to evolutions in equipment, doctrine, and training as well. In adapting to an evolving enemy, meeting the nation’s defense strategy, and fielding new items like vehicles, weapon systems, unmanned aircraft, and body armor, the Army has continuously refined its approach to how modular formations train and fight. It is within this overarching context, and the realities of new, constrained budgets, that the Army is assessing the optimal modular designs with which to fight and win future wars.

In FY 2012, the Army completed its MFI with the conversion of the final support brigade formations and the decision to defer conversion of two brigades in Europe until after the program budget review for FY 2013 (PBR 13). Through the MFI, the Army achieved a common, combat-proven organizational design of equal or better combat effectiveness compared to previous divisional brigades. The MFI creates units of common organizational design and, coupled with Army's growth since 2007, has increased the number and agility of available BCTs to meet operational commitments by simplifying and streamlining the composition of brigade-based combat and support formations. This, in turn, enhances their ability to contribute to joint, interagency, and multinational efforts. The Army continues to evaluate lessons learned and apply changes to modular force designs based on operational experience. Additionally, the Training and Doctrine Command assesses all facets of the modular force in training and combat review and evaluates modular force doctrine, training, leader development, and battle command.

By the end of FY 2012, the Army completed modular conversions for 43 of its 45 AC BCTs. Conversion of the two legacy brigades in Europe was postponed with the release of PBR 13. A subsequent decision has been made to inactivate those brigades as part of the Army's scheduled drawdown. In FY 2005, the ARNG began its transformation with an accelerated plan that allows early conversion to the new BCT designs. Transformation for an ARNG BCT can take as long as 48 months; however, by the end of FY 2011, the ARNG had successfully completed the full conversion of all 28 BCTs to a modular design. The ARNG BCTs are continuing to modernize in order to maintain interoperability with their AC counterparts.

**TABLE 10. BCT Transformation Summary<sup>1</sup>**

	FY 2008 <sup>2</sup>	FY 2009 <sup>2</sup>	FY 2010 <sup>2</sup>	FY 2011 <sup>2</sup>	FY 2012
AC Transformed	40	42	43	43	43
ARNG Transformed	28	28	28	28	28
<b>Total Transformed</b>	68	70	71	71	71
AC Transforming	2	3	1	1	0
ARNG Transforming	28	21	14	0	0
<b>Total Transforming</b>	30	24	15	1	0
<b>Total Transformation</b>	98	94	86	72	71

*Note 1: Transformed means the unit has completed its initial reorganization and re-equipping to a modular design within resource constraints, is participating in the ARFORGEN process, and may be used against a requirement. Transforming means the unit is still undergoing initial reorganization and re-equipping to a modular design within resource constraints. The last 2 Army brigades (numbers 70 and 71) do not begin transformation until 2nd Quarter, FY 2013 and 1st Quarter, FY 2014, respectively, and are not counted in this table.*

*Note 2: The prior year numbers displayed in the FY 2011 Table 10. BCT Transformation Summary, have been updated to reflect the current information.*

### ***Providing Advanced Technologies***

The Army's Science and Technology (S&T) mission is to foster invention, innovation, and the use of new technologies to leverage future force capabilities while exploiting opportunities to apply new technology capabilities to the current force. The Army depends on its S&T program to research, develop, and demonstrate high pay-off solutions to hard problems faced by Soldiers in the ever-changing, complex, global environments across the spectrum of conflict.



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The S&T community, in concert with combat developers in the Army's Capabilities Integration Center and across the entire command, place great emphasis on demonstrating evolving advanced capabilities rather than on maturing current, isolated technologies. The foundation of this effort is a strong basic research program. Investments in basic research are critical to acquiring new knowledge in areas that hold great potential to advance operational capabilities, Army-wide. The conceptual knowledge and know-how that the S&T community mines, develops, and leverages will enable revolutionary advances and ensure paradigm-shifting, future operational capabilities. The S&T strategy is designed to place advanced capabilities in the hands of small units and the individual Soldier. In doing so, it depends on a strengthened partnership among the S&T, acquisition and requirements communities, the Army leadership, and Soldiers.

The Army is also partnering with other services, combatant commands, and agencies in the Joint Capability Technology Demonstration Program to rapidly transition mature technologies into solid warfighter capabilities.

Science and technology investments support Army modernization goals of developing and fielding affordable equipment by fostering technology-based invention and innovation. As it continues to diligently identify and harvest technologies suitable for transforming the force, it is ever vigilant of potential and emerging threats.

The S&T community is sharpening research efforts to focus the core capabilities needed for the future and to identify promising leap-ahead technologies that will redefine existing paradigms of understanding. Ultimately, the focus of its work is Soldiers; it consistently seeks out new scientific avenues through which to increase their capabilities and ensure their technological superiority—today, tomorrow, and beyond.

### *LandWarNet Operational Capabilities and Focus*

Over the past decade, the Army has transitioned to a continental United States (CONUS)-based expeditionary force and, as such, access to reliable, trusted information has become a critical aspect to mission success. Whether deploying to an austere theater of operations or responding to a humanitarian crisis, the Army is heavily reliant upon a robust infrastructure and services network that supports both warfighting and global business operations. The goal is to have a completely integrated, secure, accessible, interoperable, and affordable network providing information to Soldiers and mission partners when they need it, in any environment—from garrison to the tactical edge. The current focus is an enterprise approach, Army-wide, that will align communications requirements, technology priorities, and investment strategies with the ARFORGEN and operational capability set management. The envisioned goal is a network that will provide the most effective infrastructure and services for both the warfighter mission and business support operations.

Over the past year, the focus of attention has continued to be on Army data centers and enterprise services, most notably enterprise e-mail. These initiatives are essential to the initial phases of building the network. The Army Data Center Consolidation Plan strategically consolidates data centers and applications, provides enterprise hosting as a managed service, and improves the security of Army information assets. The Defense Information Systems Agency-hosted DoD enterprise e-mail provides the Army unclassified and classified e-mail services from a managed services provider. Using DoD smartcard authentication, it allows access to e-mail at any time, from any location, and it has achieved more than a 1,000 percent increase in mailbox size. Both initiatives are significant for their cost-saving benefits and for advancing transformation of the Army's network.

### *Developing the Network of 2020*

The Army plans to incrementally modernize LandWarNet so that by 2020 it functions as a single, centrally managed, end-to-end network that is less complex; provides assured, secure access; supports joint operations; and enables an expeditionary Army that can train as it fights. The intent is to make network development, operation, and sustainment easier, more efficient, and more cost-effective while improving the Army's cyber-security posture and providing optimal support to operations and business processes.

LandWarNet modernization hinges on four key objectives: building capacity; improving cyber security; providing end-to-end enterprise services; and implementing network standards.

Increased capacity is essential to the end-to-end network initiatives that support enterprise services and centralized network management. The Army will increase bandwidth; increase path diversity to improve network capacity and data throughput; and modernize technical infrastructure on posts, camps, and stations (P/C/S). Increased P/C/S capacity will also support the Secret Internet Protocol Router Network, allied mission network, and integrated training environment.

With rapidly increasing cyber threats, LandWarNet must protect and disseminate information from the top down and the bottom up. Security requirements call for improved visibility of the entire network and its real-time status as well as the ability to manage every device residing on the network in order to reduce the risk of attack. Major security initiatives include identity, credential, and access management, which aligns with federal and DoD regulations and guidance. The Army is also implementing thin- or zero-client computing to limit local storage of information and help secure the network. With thin- or zero-client computing, desktop, laptop, or mobile devices serve as viewers to access information residing in secure facilities. Other security initiatives include information technology asset management, allowing the Army to monitor and manage all devices connected to the network for security, vulnerabilities, and access control.

In modernizing the network, the Army will expand enterprise services to simplify and extend access to data, applications, collaboration tools, and communications. It will provide current and new services, Army-wide, such as enterprise content management and collaboration services, as well as voice, video, chat, and other capabilities. The elimination of stovepipe video and telephone systems will reduce costs and provide access to critical information and capabilities. In part, enterprise services will be enabled through cloud computing, which provides on-demand access to resources such as servers and applications, while supporting cost-effective access anytime, anywhere. The Army baseline IT services establish standards for enterprise IT services, making it easier to consistently operate and maintain

infrastructure on Army installations and to perform installation-level tasks and functions for service delivery. The Army Enterprise Service Desk initiative will use an enterprise service management approach to simplify issue and problem resolution and reduce the number of help desks required across the Army.

Developing and implementing effective network standards is fundamental to all aspects of network modernization. The LandWarNet must be integrated with the DoD joint information environment (JIE) and its enterprise architecture must be consistent with JIE. The Army is also leveraging the JIE-compatible common operating environment (COE), which defines technical standards for computing environments from enterprise servers to mobile devices. The COE promotes the use of commercial-off-the-shelf technology, embraces a non-proprietary data transmission mode called Everything over Internet Protocol, and enables rapid insertion of new technologies and interoperability with mission partners. Alignment with the COE is mandatory for new systems and capabilities and the Army is working to bring existing programs of record and other systems into compliance. The Army is also standardizing network operations to unify the operations and security of both tactical and enterprise-level network operations.

LandWarNet modernization will result in a more resilient, affordable, available, responsive, and defensible network that improves the Army's overall ability to accomplish its mission, while gaining efficiencies and streamlining processes in a fiscally-constrained environment.

The projected savings from enterprise e-mail, which are identified in an Army Audit Agency audit report, are \$379.9 million for FY 2013 to FY 2017. The report was part of an Army response to the FY 2012 NDAA language. The Army is not expecting to realize savings for consolidating the data centers until after FY 2016.

During FY 2012, the Army has completed, or is in the process of completing, the following activities to set the stage for implementation of the Network of 2020:

- Published the common operating architecture and implementing instructions.
- Developed the requirement for establishing Army enterprise collaboration capability.
- Continued to implement enterprise e-mail and data center consolidation.
- Continued to ensure that the Network of 2020 is aligned with JIE capability which is being worked by the Joint Staff, J-6 (Command, Control, and Communications).



A Soldier backs an M32 Bradley fighting vehicle into a C-17 cargo bay for transport back to Fort Benning, GA. U.S. Air Force photo by Tech. Sgt. Michael OHalloran

### *Developing Force Generation Platforms in Support of Army Force Generation*

The FY 2012 saw the Army improve its ability to out-load power projection platforms from CONUS, most notably through the launch of the Rapid Expeditionary Deployment Initiative (REDI). The deployments of recent years have been deliberate, allowing deploying units to plan well in advance. However, the Army recognizes the need to restore the ability to project power on little-to-no notice, and REDI, as part of the Army Power Projection Program (AP3), is the initiative to do so. A total of 15 military construction projects were completed, are ongoing, or have been initiated to support REDI during FY 2012.

Of the 15 projects, 7 were ongoing from FYs 2010 and 2011. The first project, a rail head upgrade and expansion project at Fort Carson (CO), improves the out-loading of a heavy BCT from the current 240 railcars per day to the required 275 railcars per day. This project constructs five additional spurs to handle the growth at Fort Carson as documented in the Grow the Army Stationing Plan. The project was completed in February 2012.

The next three projects improve out-loading at the Charleston Naval Weapons Station (SC)—the only military general cargo seaport in the southeast region. This seaport has been busy supporting current operations in the Middle East for both deployment and redeployment. The first of these three projects upgrades the port's paving, lighting, and fencing to improve security for equipment and personnel during deployment and

also to help protect equipment from damage. The project is at 90 percent completion and is expected to be finished in July 2013. The second of the three projects upgraded rail capabilities from 40 railcars per day to 60 railcars per day to fully meet rail requirements. This project was completed in February 2012. The third project expands the pier and hardstand to adequately position larger roll-on and roll-off and container ships. This project is 55 percent completed, with a projected completion date of July 2013. Both the paving, lighting, and fencing project and the pier and hardstand project were delayed from their original calendar year (CY) 2012 completion dates due to the removal of unexploded ordnance. This action is ongoing, and the revised dates are within the required completion window.

The next two projects were for construction of a consolidated multi-class munitions handling, storage, and shipping facility and a depot level ammunition igloo at McAlester Army Ammunition Plant (AAP) (OK). These projects corrected ammunition, shipping, receiving, and storage deficiencies to provide more efficient and timely out-loading and ample ammunition storage, especially for small quantity shipments, which experienced a 50 percent increase in recent years. Both projects were completed in CY 2012.

The seventh project is the construction of a staging area complex at Fort Bragg (NC). This complex consolidates staging area activities for efficiently deploying airborne units to meet global response force requirements; it is funded through the Grow the Army initiative. The project is 75 percent completed, with anticipated completion scheduled in January 2013.

The remaining eight projects were newly initiated in FY 2012. The first two of these projects are at the McAlester AAP. One will upgrade the mainline rail line serving the McAlester AAP from 90-pound steel rail to 115-pound steel rail in order to accommodate modern heavy rail equipment. Failure to replace the rail would have resulted in an unserviceable rail line and contributed to delays in shipping ammunition to Soldiers. The other project involves constructing a concrete pad extension from the ammunition magazines to truck parking areas. Currently, ammunition loading onto trucks requires double-handling (forklift to small truck to loading dock transfer area to large truck). This project will allow direct loading from the forklift to large trucks. Both projects were initiated in FY 2012; the mainline rail project is 25 percent complete, and the AP3 ammunition pad extension is 50 percent completed. Both projects are scheduled for completion by July 2013.

The next new project is a ready building at Forbes Field supporting air deployments at Fort Riley (KS). Current facilities will not adequately handle the increase of Soldiers plus equipment, which is documented in the Grow the Army



Stationing Plan. When completed, the ready building will process Soldiers and equipment air-deploying and redeploying to-and-from Fort Riley. Work has just begun, and project completion is expected in April 2013.

The next three projects are new rail projects at Fort Benning (GA); Fort Sill (OK), and Camp Atterbury (IN). The new Fort Benning rail improvements increase railcar storage capacity so that railcars do not require call-up from commercial railyards (some up to 100 miles away). Increased on-installation railcar storage will increase rail out-loading efficiency from 144 railcars per day to the full-up 183 railcars per day for a three-day heavy BCT load-out. The Fort Sill rail upgrade constructs a railroad wye, which allows railcars to be turned around on-post. Railcars laden with equipment received at night must be correctly oriented for offloading (rail safety procedures do not allow equipment to back off railcars). If the railcars are oriented in the wrong direction, the commercial rail company serving Fort Sill must return to reorient the railcars as there is no way to turn railcars around at Fort Sill. Project award occurred in April 2012 with a scheduled completion date of August 2013. The third rail project upgrades a railhead at Camp Atterbury from a 40-railcar per day capability to the required 120-railcar per day capability, thereby supporting the new power generation platform to adequately outload mobilizing BCTs. This project was just recently awarded; project completion is May 2014.

The final two projects construct deployment processing centers (DPC) at Camp Atterbury and at Camp Shelby (MS). These installations were recently designated as power generation platforms and, as such, now deploy Soldiers and equipment of mobilizing BCTs. The new DPCs were necessary to handle processing of Soldiers and equipment. Work on both projects has just begun, and completion is anticipated in October 2013 for the Camp Shelby DPC, and May 2014 for the Camp Atterbury DPC.

### ***Implementing Base Realignment and Closure/Restationing Forces***

Base Realignment and Closure (BRAC) 2005 provided an unprecedented one-time opportunity for reshaping how the Army trained, deployed, supplied, equipped, and stationed its Soldiers, Civilians, and their Families to better support combatant commanders in confronting the security challenges facing the nation. A key enabler of Army transformation, BRAC 2005 was fully synchronized with other Army stationing initiatives such as global defense posture realignment, Grow the Army, and Army modular forces. The BRAC also closed installations and leased facilities that were either no longer relevant or were less effective in supporting a joint and expeditionary Army. In partnership with other services, the Army used BRAC 2005 to transform RC infrastructure to create more operational opportunities for joint

training and deployment. This transformation created efficiencies in core Army business processes.

Under BRAC 2005, the Army closed 10 major and 1 minor installations, 387 RC installations, and 8 leased facilities. Additionally, it realigned 53 installations or functions and enabled the Army to establish multi-component headquarters, joint Army training centers of excellence, joint bases, joint power projection platforms, a human resources center of excellence, and joint technical and research facilities. To accommodate the relocated units from the closed RC installations, BRAC 2005 authorized 125 new multi-component armed forces reserve centers and realigned the USAR command and control structure.

With an investment of \$17.8 billion during the FY 2006-2011 implementation period, the BRAC 2005 was more than three times larger than all four previous BRAC rounds combined, and represented 51 percent of the overall DoD BRAC 2005 program. The BRAC's operational efficiencies, combined with the divestiture of excess infrastructure, produced \$1.0 billion in annual net recurring savings for reinvestment in enduring Army missions. The BRAC 2005 represented an unparalleled recapitalization of the Army's infrastructure funding of 329 major construction projects valued at \$13.5 billion.

The Army completed the conveyance of approximately 46 percent (23,372 acres) of all BRAC 2005 excess property before the 15 September 2011 deadline. In prior BRAC rounds, property disposal and the resulting savings were largely left until after the six-year implementation period was complete. Caretaker activities for remaining BRAC 2005 installations will continue until environmental restoration is completed and all remaining excess property is conveyed.

### ***Implementing Business Transformation Initiatives***

Beginning in 2009, the Secretary of the Army, acting through the chief management officer, has been responsible for carrying out an Army business transformation initiative. The Secretary established the Office of Business Transformation (OBT) to concentrate on achieving business process improvements. The OBT's objectives follow:

- Transform business operations.
- Improve the effectiveness and efficiency of business processes.
- Transform business systems information technology.
- Promote resource-informed decision making.
- Achieve integrated management.

These objectives will culminate in an adaptive generating force that better supports an agile and versatile operating force. They are also expected to successfully prioritize, balance, and integrate Army activities and resources in the present and posture them for future success. An integrated management system focuses on results, with an emphasis on cutting costs while modernizing a mission-ready force—a readiness at best value rather than readiness at any cost approach.

During FY 2012, the continuous performance improvement (CPI)/LSS element within the OBT continued to provide enabling activities to the Army's business transformation and the Secretary of the Army's reformation of the generating force. All efforts support the strategic guidance and direction of the Army's chief management officer. The CPI/LSS community has focused its efforts on Army-wide performance improvement. Operational benefits realized in logistics throughput in Afghanistan and Iraq (US CENTCOM's CPI/LSS activities) are having direct effects on our warfighters and are achieving better performance and financial benefits within the generating force.

In FY 2012, the OBT CPI/LSS element was able to better connect the outcomes of CPI/LSS projects contained in the Army's project management database, PowerSteering, with the financial management activities inherent in building the Army's POM. This was achieved in concert with the staffs of the Assistant Secretary of the Army for Financial Management and Comptroller (ASA(FM&C)) and the Deputy Assistant Secretary of the Army for Cost and Economics. The CPI/LSS continues to be a rigorous, proven methodology to achieve performance improvement at any level. In FY 2011, the 1,186 projects completed across all Army commands—to include the RC—have potentially yielded \$8.4 billion in total financial benefits, of which \$2.3 billion are savings. The Army's program relies on training CPI/LSS practitioners who return to their units to tackle leadership-supported projects. In FY 2012, the CPI/LSS community trained 1,264 new practitioners, from entry level experience through enterprise-level expertise, to support Army business transformation and assist in the reform of its generating force.

On 1 July 2012, the Army completed deployment of the General Fund Enterprise Business System (GFEBS). It is the centerpiece of the Army's financial system transformation effort as it provides the core capability to support an unqualified audit opinion of the Army's General Fund. In addition, the GFEBS transforms business processes to enable better-informed decisions, better-managed resources, and better support to the warfighter. The GFEBS integrates funding, real property management, financial accounting, cost management and related output, and performance data in an enterprise resource planning system.

The system is central to the Army's transitioning to a cost and performance culture.

The GFEBS is a web-based system used by the AC, the ARNG, and the USAR. With the deployments in FY 2012, GFEBS is now operational across 27 commands, at more than 200 locations, and in 71 countries. The FY 2012 deployment added:

- Organizations in Kuwait, Qatar, and Afghanistan as well as in the United States.
- Over 17,000 new users—bringing the total to over 52,000.
- Over \$49 billion in budgetary allotment—bringing the total allotment to over \$80 billion.

The GFEBS is enabling the Army to comply with the wide range of statutory and regulatory requirements—the Federal Financial Management Improvement Act, the U.S. Standard General Ledger, accounting standards, and the DoD Standard Financial Information Structure. It is also enabling the Army to retire old, stand-alone systems.

The GFEBS is the key element in retiring systems in the financial domain. The Army has retired 13 systems in FY 2012, bringing the total retired systems to 31 as of this year. The Army continues to transform; its cost and performance culture requires that leaders understand and incorporate cost considerations in their planning and decision-making processes—an approach that will enable the Army to achieve its readiness and performance objectives more efficiently and effectively.

To cultivate a cost culture, the Army is executing education and training programs for military and civilian personnel at all levels, supporting both the resource management and functional communities. It also established the graduate-level Cost Management Certificate Course (CMCC) to educate and develop cost-savvy subject matter experts to serve as senior leader staff advisors.

The Army trained 103 students in the CMCC in FY 2012, and, in the same fiscal year, the ASA(FM&C) developed and piloted a new course in cost-benefit analysis (CBA). The CBA training course provides rigorous, analytical instruction, opportunities for hands-on application in performing CBA, and one-on-one evaluation of work. Selected graduates will create a cadre of certified trainers in the field to propagate CBA concepts. In FY 2013, the principles of cost analysis and management and intermediate cost analysis and management courses will be offered for the first time by resident and mobile Training and Doctrine Command training teams. The Army continued to offer CBA introductory training during FY 2012 to enable

and advance resource-informed decision making. Nearly 500 individuals completed the training in FY 2012 to bring the total trained, since February 2010, to more than 2,800. Cost Management 101 training has been designed to educate Soldiers and civilians working at GFEBS sites about cost management principles in advance of system deployment. This training will continue to be delivered to the Army users. As the Army continues to emphasize the importance of cost management principles and skills, it is exploring a Cost Management Fellowship Program to formally identify and recognize cost management best practices as well as the cost management functional skills that support them.

## Conclusion

Looking to the future, the Army is highly-focused on three main areas.

- Its first priority remains supporting operations in Afghanistan.

- Second, it is striving to reform its acquisition process and ensure energy security. Army institutions and functions—from personnel to training and development to materiel systems—must have the same unparalleled ingenuity, flexibility, and adaptability as operational forces. The Army's acquisition system is also in need of significant reform, to become more agile, flexible, economical, fair, and effective.
- And third, the Army will spare no effort to incorporate the principles, processes, and practices that preserve Soldier readiness and capability. As it reduces its size and footprint, the Army is right-sizing its formations to build the right number of units, with the right capability, to meet the evolving needs of the joint force. The past 10 years have taught the nation that an operational reserve force is essential to accomplishing Army missions and allowing it to expand rapidly when faced with the need to do so. Toward that end, the Army is committed to investing deliberately and wisely in its Soldiers, Families, and Civilians to make sure they are prepared and supported.



Walking to prepare a truck for a mission to support initiatives that will ensure the sustainability of Afghan agricultural productivity. Photo courtesy of the U.S. Army.



A Soldier provides security during a patrol to Black Rock, Khowst Province, Afghanistan. Photo courtesy of the U.S. Army.

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## MANAGEMENT ASSURANCES

Commanders and managers throughout the Department of the Army annually ensure the integrity of their reporting systems, programs, and operations. This section focuses on the Army's system of internal controls to comply with such laws as the Federal Financial Management Improvement Act (FFMIA) of 1996 and the Federal Financial Manager's Financial Integrity Act of 1982. The requirements promote the production of reliable, timely, and accurate financial information through efficient and effective internal controls. By having effective internal controls, the Army is able to improve efficiency, operating effectiveness and enhance public confidence in Army stewardship of public resources.

### Chief Financial Officer Compliance

The passage of the Chief Financial Officers (CFO) Act of 1990 required major federal agencies to prepare audited financial statements for the first time. In 1994, the Government Management Reform Act extended the CFO Act to include agency-wide reports from all major executive branch agencies and their components. The Government Performance and Results Act of 1993 required agencies to systematically report on plans and performance. The FFMIA of 1996, along with the Clinger-Cohen Act of 1996 (also known as the Information Technology Management Reform Act), required that agencies install integrated systems that comply with federal accounting standards and produce auditable financial statements in accordance with Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*. Additionally, agencies must follow generally accepted accounting principles formulated by the Federal Accounting Standards Advisory Board.

### Internal Controls

The Army operates a robust manager's internal control program in compliance with OMB Circular A-123 to employ a comprehensive system of continuous evaluation of internal controls. The Army's program is fully integrated with functional program control assessments. In strict adherence to the Office of the Under Secretary of Defense (Comptroller) guidance, the Army reports a level of assurance over its internal controls in three distinct areas: internal controls over non-financial operations, internal controls over financial reporting, and internal controls over financial systems. See the complete Army Statement of Assurance at <http://asafm.army.mil/offices/FO/IntControl.aspx?OfficeCode=1500>

### Internal Controls Over Financial Reporting

As stated in the Army's Annual Statement of Assurance dated August 8, 2012, "Although we continue to make progress in improving internal controls over financial reporting for the General and Working Capital Funds, I cannot provide assurance that the Army's internal controls for financial reporting were operating effectively as of June 30, 2012. This assessment is based on the auditor's inability to render an audit opinion; numerous uncorrected actions identified in our financial improvement plan; 13 weaknesses associated with the General Fund; and nine weaknesses associated with the Working Capital Fund."



## ANALYSIS OF FINANCIAL STATEMENTS

As discussed in the accompanying independent auditor's reports, long-standing financial management challenges prevent the Army from producing auditable financial statements for the Army General Fund (Army GF) or the Army Working Capital Fund (Army WCF). The Army, however, continues to work with the DoD to develop sustainable business practices and enhanced internal controls to improve financial management processes and produce quality financial management information. These processes must be supported by compliant business systems and an effective set of management controls.

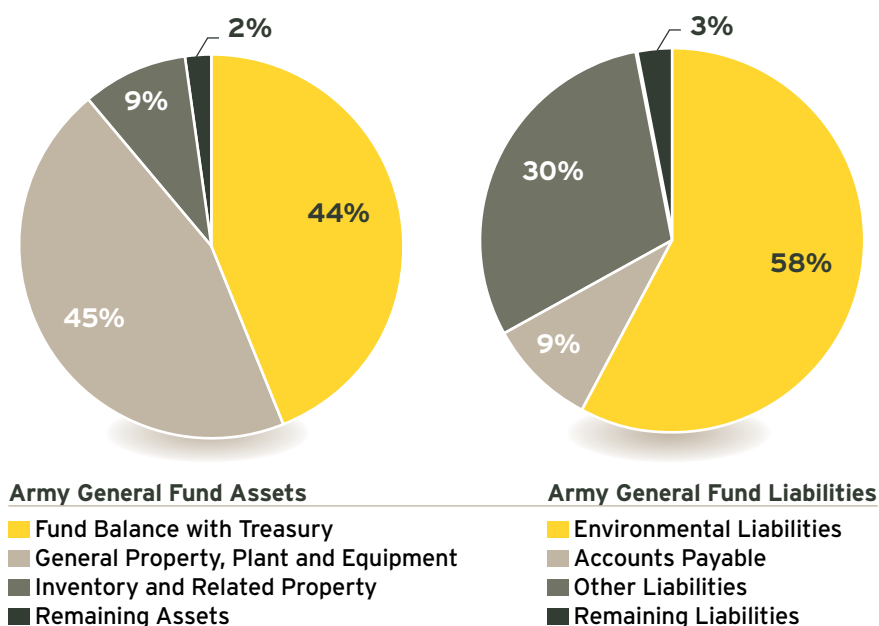
### Army GF Financial Results and Balance Sheet

The Army GF Balance Sheet includes total assets that exceed \$352.1 billion. Two asset categories, Fund Balance with Treasury and General Property, Plant and Equipment (GPP&E), comprise 89 percent of total assets, with values of \$153.3 billion and \$160.0 billion, respectively.

Liabilities primarily consist of \$30.4 billion in Environmental Liabilities and \$4.9 billion in Accounts Payable.

The GPP&E account decreased \$11.9 billion due to adjustments made to the Army GF's mission critical assets as a result of the Army's ongoing audit readiness efforts.

**FIGURE 3. Composition of GF Assets and Liabilities**



**TABLE 11. Select GF Assets and Liabilities**

ASSET TYPE (Amounts in billions)	FY 2011	FY 2012	Change	Percentage of FY 2012 Assets
Fund Balance with Treasury	\$166.9	\$153.3	(\$13.6)	44%
General Property, Plant and Equipment	171.9	160.0	(11.9)	45%
Inventory and Related Property	31.2	30.8	(0.4)	9%
Remaining Assets	11.6	8.0	(3.6)	2%
<b>Total Assets</b>	<b>\$381.6</b>	<b>\$352.1</b>	<b>(\$29.5)</b>	<b>100%</b>

*Amounts may not sum due to rounding.*

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LIABILITY TYPE (Amounts in billions)	FY 2011	FY 2012	Change	Percentage of FY 2012 Liabilities
Environmental Liabilities	\$31.8	\$30.4	(\$1.4)	58%
Accounts Payable	8.6	4.9	(3.7)	9%
Other Liabilities	14.4	15.4	1.0	30%
Remaining Liabilities	1.3	1.5	0.2	3%
<b>Total Liabilities</b>	<b>\$56.1</b>	<b>\$52.2</b>	<b>(\$3.9)</b>	<b>100%</b>

*Amounts may not sum due to rounding.*

## Army WCF Financial Results

The Army WCF activities maintain the Army's combat readiness by providing supplies, equipment, and ordnance to prepare, sustain, and reset our forces in the most efficient and cost-effective manner possible. In performing this mission, WCF activities are obligated to control and minimize costs. Financial performance is measured through cash management, net operating results (NOR), and accumulated operating results (AOR). Operational performance is measured by carryover, stock availability, and production.

## Cash Management

The current balance of funds with the U.S. Treasury equals the beginning of the fiscal year amount plus the cumulative fiscal-year-to-date amounts of collections, appropriations and transfers-in, minus the cumulative fiscal year-to-date amounts of disbursements, withdrawals and transfers-out. The Army WCF is required to maintain a positive cash balance to prevent an Antideficiency Act violation under 31 USC, § 1517(a), *Prohibited Obligations and Expenditures*. Unlike appropriated funds, the Army WCF cash balance is not equal to outstanding obligations; however, the cash-on-hand at Treasury must be sufficient to pay bills when due.

Sufficient cash levels should be maintained to support 7 to 10 days of operational disbursements, plus adequate cash to meet 6 months of capital investment program disbursements, plus the amount of any positive accumulated operating results that is to be returned to customers.

The cash balance is primarily affected by cash generated from operations; however, the balance is also affected by appropriations, transfers, and withdrawals. Maintaining a proper cash balance depends on setting rates to recover full costs—including prior year losses—accurately projecting workload and meeting established operational goals. The Army WCF ended FY 2012 with a cash balance of \$1,334.5 million, within the 7- to 10-day balance requirement.

Table 12 shows an overall growth in cash primarily from operations and direct appropriations offset by transfers out. The Army WCF received direct appropriations for war reserve materiel.

**TABLE 12. Army WCF Cash**

(Amounts in millions)	FY 2010	FY 2011	FY 2012
Beginning Cash	\$1,349.6	\$1,808.1	\$1,900.5
Collections	\$16,315.9	\$13,742.5	\$12,897.2
Disbursements	15,627.0	13,004.8	12,478.2
Net Disbursements and Collections	\$688.9	\$737.8	\$419.0
Appropriations Received	50.0	54.6	155.2
Transfers Out	280.3	700.0	1,140.2
Net Cash Transactions	\$458.6	\$92.4	(\$566.0)
Ending Cash	\$1,808.1	\$1,900.5	\$1,334.5

*Amounts do not sum due to rounding to match principal financial statement amounts.*

### Net Operating Results and Accumulated Operating Results

The NOR represents the difference between revenues and costs within a fiscal year. The AOR represents the aggregate of all recoverable net earnings, including prior-year adjustments, since inception of the Army WCF. The goal of the Army WCF is to establish rates that will bring the AOR to zero in the budget year. An activity group's financial performance is measured by comparing actual results to the budget's NOR and AOR.

**TABLE 13. Net and Accumulated Operating Results by Activity Group**

OPERATING RESULTS (Amounts in millions)	FY 2010	FY 2011	FY 2012
Industrial Operations NOR	\$57.3	\$113.8	\$42.0
Industrial Operations AOR <sup>1</sup>	\$525.6	\$639.4	\$681.5
Supply Management NOR	(\$125.1)	(\$103.1)	(\$207.5)
Supply Management AOR	\$335.0	\$231.9	\$24.4

*Note 1: Includes prior-period AOR adjustments*

### Carryover

Carryover is the dollar amount of orders accepted from customers that have not been completed by the end of a fiscal year. It is a normal part of doing business. These orders enable the industrial workforce to maintain continuity in production operations. The Army expects the carryover for FY 2012 to be less than the maximum allowable amount. The figures shown for FY 2012 in the table below are estimates.

### Stock Availability

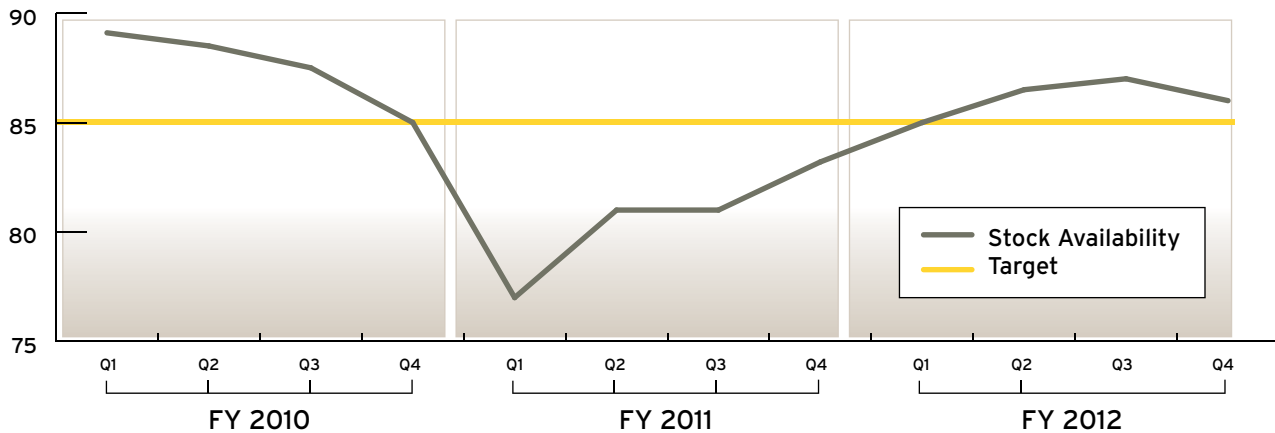
Stock availability measures the percentage of requisitions filled within established timeframes. The DoD and Army have set a target of 85 percent stock availability. The Army anticipates to exceed this goal in FY 2012.

**TABLE 14. Army WCF Carryover**

(Amounts in millions)	FY 2010	FY 2011	FY 2012
New Orders	\$6,196.5	\$7,262.5	\$5,466.5
Allowable Carryover <sup>1</sup>	\$4,075.5	\$4,684.2	\$ 4,763.8
Calculated Carryover <sup>1</sup>	\$3,452.0	\$4,321.2	\$ 4,573.3

*Note 1: FY 2012 amounts are estimated.*



**FIGURE 4. Stock Availability (percentage)**

### Production

Although the Industrial Operations Activity Group (IOAG) is comprised of 13 activities, the preponderance of workload is performed at the five hard-iron maintenance depots. Major operations in Afghanistan place tremendous demands on equipment. As a result of the higher operating tempo, rough desert environments, and limited depot maintenance available in theater, operational fleets age at a far greater pace than expected. To counter this, the Army established a reset program designed to reverse the effects of combat stress on equipment and to prepare equipment for future missions. Industrial operations received \$1,430 million in reset orders, representing approximately 26 percent of FY 2012 new orders.

The Army's depots and their efforts to partner with industry are critical to the entire reset effort. These repair programs must continue through the end of the current conflict and for at least three additional years to reconstitute equipment completely. Due to actions taken in support of wartime requirements, the IOAG significantly increased depot production over pre-war levels, as illustrated in Table 15.

The aircraft increase shown in the FY 2012 column of Table 15 is due to increases in production requirements. The increase to the annual production throughput of high mobility, multipurpose-wheeled vehicles (HMMWV) from FY 2011 to FY 2012 is due to the HMMWV Recap program. Track shoe production levels decreased from FY 2010 to FY 2012 due to a decrease in expected operational levels for the M1 and Bradley fighting vehicles. The drop in production results from the customer decreasing the requirements and is not related to any production issues.

**TABLE 15. Annual Production Throughput<sup>1</sup>**

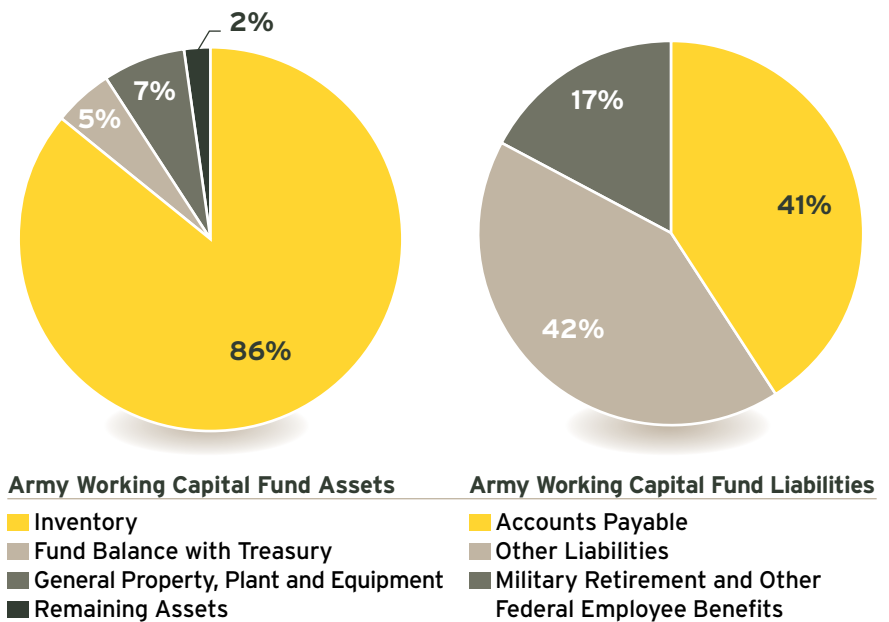
	Pre-War	FY 2010	FY 2011	FY 2012
Aircraft	4	74	101	106
Helicopter Engines	<200	468	760	832
Bradleys	144	758	349	317
HMMWVs	<100	6,189	2,090	2,480
Firefinder Radars	<1	61	31	37
Track Shoes	120,000	120,667	39,161	25,136

*Note 1: Throughput is the number of weapon systems completed for any given year.*

### Army WCF Balance Sheet

The Army WCF balance sheet shows assets exceeding \$25.8 billion, primarily in Inventory and Fund Balance with Treasury. Liabilities consist of Accounts Payable and Other Liabilities, which include payroll, benefits, accrued annual leave, and workers compensation.

**FIGURE 5. Army WCF Assets and Liabilities**



**TABLE 16. Army WCF Assets and Liabilities**

ASSET TYPE (Amounts in millions)	FY 2011	FY 2012	Change	Percentage of FY 2012 Assets
Inventory	\$25,211.5	\$22,096.5	(\$3,115.0)	86%
Fund Balance with Treasury	1,900.5	1,334.5	(566.0)	5%
General Property, Plant and Equipment	1,564.4	1,748.8	184.4	7%
Remaining Assets	908.9	626.7	(282.2)	2%
<b>Total Assets</b>	<b>\$29,585.3</b>	<b>\$25,806.5</b>	<b>(\$3,778.8)</b>	<b>100%</b>

*Amounts may not sum due to rounding.*

LIABILITY TYPE (Amounts in millions)	FY 2011	FY 2012	Change	Percentage of FY 2012 Liabilities
Accounts Payable	\$783.4	\$502.1	(\$281.3)	41%
Other Liabilities	644.5	528.0	(116.5)	42%
Military Retirement and Other Federal Employee Benefits	221.6	215.1	(6.5)	17%
<b>Total Liabilities</b>	<b>\$1,649.5</b>	<b>\$1,245.2</b>	<b>(\$404.3)</b>	<b>100%</b>

*Amounts may not sum due to rounding.*

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## REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION AND REQUIRED SUPPLEMENTARY INFORMATION

Stewardship information relates to expenditures involving a substantial investment by the Army for the benefit of the nation. When made, these expenditures are treated as expenses in the financial statements. Since these expenses are intended to provide long-term benefits to the public, they are reported as supplemental information in the financial statements<sup>1</sup>. There are four reported areas for stewardship information: (1) nonfederal physical property; (2) investments in research and development (R&D); (3) deferred maintenance; and (4) heritage assets and stewardship land.

Investment in nonfederal physical property is an expense incurred by the Army for the purchase, construction, or major renovation of physical property owned by state and local governments. An example of this type of investment is funding provided to the Army National Guard (ARNG) for assistance in the construction of an ARNG facility on state land. Since the facility is constructed on state land, it is the property of the state; therefore, the Army cannot report it as an asset. However, since the funds were used to acquire a mission-related state facility, the outlay is tracked as an investment in nonfederal physical property.

Investments in R&D are based on R&D outlays (expenditures). Outlays are used because current Army accounting systems are unable to capture and summarize costs in accordance with federal accounting standards. The R&D programs are classified as basic research, applied research, and development.

Stewardship information is also comprised of real property and military equipment deferred maintenance. Real property deferred maintenance relates to maintenance needed on Army facilities that has not been funded. At the end of FY 2012, the Army reported approximately \$37.2 billion in deferred real property maintenance on facilities with a replacement value of approximately \$254.2 billion. Real property deferred maintenance totals approximately 15 percent of estimated replacement value of the facilities requiring maintenance. The 10 major categories of military equipment deferred maintenance totaled approximately \$307.4 million at the end of FY 2012. Electronic and communication systems equipment represented the largest category of deferred equipment maintenance at approximately \$144.5 million.

Heritage assets are comprised of property, plant and equipment (PP&E) of historical, natural, cultural, educational, or artistic significance. Specifically, the Army's heritage assets are comprised of buildings and structures, archeological sites, museums, and museum collection items. Stewardship land is land other than that acquired for, or in connection with, general PP&E.

Detailed information concerning most stewardship information may be found in the Required Supplementary Stewardship Information and the Required Supplementary Information (RSI) sections of this report. Heritage assets and stewardship land are no longer reported in the RSI; they are now required to be reported in a note to the statements.<sup>2</sup> Additional information on heritage assets and stewardship land may be found in Note 10 of the Army General Fund statements.

<sup>1</sup> Federal Accounting Standards Advisory Board. Statement of Federal Financial Accounting Concepts and Standards (June 30, 2010). Statement of Federal Financial Accounting Standards 8: Supplementary Stewardship Reporting, page 762. See [http://www.fasab.gov/pdf/FILES/codification\\_report2010.pdf](http://www.fasab.gov/pdf/FILES/codification_report2010.pdf).

<sup>2</sup> *ibid.* Statement of Federal Financial Accounting Standards 29: Heritage Assets and Stewardship Land, pages 9 and 13 and Technical Release 9: Implementation Guide for Statement of Federal Financial Accounting Standards 29: Heritage Assets and Stewardship Land, page 46. SFFAS 29 found at [http://www.fasab.gov/pdf/FILES/sffas\\_29.pdf](http://www.fasab.gov/pdf/FILES/sffas_29.pdf). Technical Release 9 can be found at <http://fasab.gov/aapcl/technical.html>.





## LIMITATIONS

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### *Limitations of the Financial Statements*

The financial statements have been prepared to report the financial position and results of operations for the entity, pursuant to the requirements of Title 31, United States Code, Section 3515(b).

While the statements have been prepared from the books and records of the entity, in accordance with the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity.

BUILDING ON A FOUNDATION OF  
**STRENGTH**

Fiscal Year 2012 United States Army Annual Financial Report

Department of Defense - Army General Fund

**CONSOLIDATED BALANCE SHEET**

As of September 30, 2012 and 2011 (Amounts in thousands)

	2012 Consolidated	2011 Consolidated
<b>ASSETS (Note 2)</b>		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	\$ 153,268,451	\$ 166,985,312
Investments (Note 4)	2,181	3,205
Accounts Receivable (Note 5)	353,386	538,573
Other Assets (Note 6)	434,558	888,607
Total Intragovernmental Assets	\$ 154,058,576	\$ 168,415,697
Cash and Other Monetary Assets (Note 7)	1,526,989	1,432,966
Accounts Receivable, Net (Note 5)	1,355,935	960,325
Inventory and Related Property, Net (Note 9)	30,824,075	31,180,416
General Property, Plant and Equipment, Net (Note 10)	159,971,256	171,879,899
Other Assets (Note 6)	4,339,865	7,815,573
<b>TOTAL ASSETS</b>	<b>\$ 352,076,696</b>	<b>\$ 381,684,876</b>
<b>LIABILITIES (Note 11)</b>		
Intragovernmental:		
Accounts Payable (Note 12)	\$ 1,766,162	\$ 2,028,077
Debt (Note 13)	0	1
Other Liabilities (Note 15 and 16)	1,870,937	3,109,908
Total Intragovernmental Liabilities	\$ 3,637,099	\$ 5,137,986
Accounts Payable (Note 12)	3,176,752	6,632,564
Military Retirement and Other Federal Employment Benefits (Note 17)	1,406,105	1,356,264
Employment Benefits (Note 17)		
Environmental and Disposal Liabilities (Note 14)	30,417,209	31,767,991
Loan Guarantee Liability (Note 8)	1,018	154
Other Liabilities (Note 15 and Note 16)	13,532,892	11,292,808
<b>TOTAL LIABILITIES</b>	<b>\$ 52,171,075</b>	<b>\$ 56,187,767</b>
<b>COMMITMENTS AND CONTINGENCIES (NOTE 16)</b>		
<b>NET POSITION</b>		
Unexpended Appropriations - Other Funds	\$ 147,252,857	\$ 162,359,241
Cumulative Results of Operations - Earmarked Funds	36,212	49,586
Cumulative Results of Operations - Other Funds	152,616,552	163,088,282
<b>TOTAL NET POSITION</b>	<b>\$ 299,905,621</b>	<b>\$ 325,497,109</b>
<b>TOTAL LIABILITIES AND NET POSITION</b>	<b>\$ 352,076,696</b>	<b>\$ 381,684,876</b>

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.

Department of Defense - Army General Fund

**CONSOLIDATED STATEMENT OF NET COST**

<i>As of September 30, 2012 and 2011 (Amounts in thousands)</i>	<b>2012 Consolidated</b>		<b>2011 Consolidated</b>	
<b>Program Costs</b>				
Gross Costs	\$	217,038,974	\$	227,456,499
Military Personnel		67,560,245		70,291,279
Operations, Readiness & Support		78,701,761		94,073,478
Procurement		31,216,620		37,363,041
Research, Development, Test & Evaluation		13,993,569		14,596,807
Family Housing & Military Construction		25,566,779		11,131,894
(Less: Earned Revenue)	\$	(9,875,759)	\$	(11,502,557)
Net Cost before Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	207,163,215	\$	215,953,942
Net Program Costs Including Assumption Changes	\$	207,163,215	\$	215,953,942
<b>Net Cost of Operations</b>	\$	207,163,215	\$	215,953,942

*The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.*



Department of Defense - Army General Fund

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**As of September 30, 2012 and 2011  
(Amounts in thousands)

	2012 Earmarked Funds	2012 All Other Funds	2012 Eliminations	2012 Consolidated
<b>CUMULATIVE RESULTS OF OPERATIONS</b>				
<b>Beginning Balances</b>	\$ 49,586	\$ 163,088,282	\$ 0	\$ 163,137,868
<b>Beginning balances, as adjusted</b>	\$ 49,586	\$ 163,088,282	\$ 0	\$ 163,137,868
<b>Budgetary Financing Sources:</b>				
Appropriations used	0	212,276,952	0	212,276,952
Nonexchange revenue	(45)	(461)	0	(506)
Donations and forfeitures of cash and cash equivalents	4,046	0	0	4,046
Transfers-in/out without reimbursement	0	1,140,194	0	1,140,194
<b>Other Financing Sources:</b>				
Donations and forfeitures of property	0	35,024	0	35,024
Transfers-in/out without reimbursement (+/-)	0	4,357,168	0	4,357,168
Imputed financing from costs absorbed by others	0	1,043,601	0	1,043,601
Other (+/-)	8,778	(22,187,146)	0	(22,178,368)
<b>Total Financing Sources</b>	\$ 12,779	\$ 196,665,332	\$ 0	\$ 196,678,111
<b>Net Cost of Operations (+/-)</b>	26,153	207,137,062	0	207,163,215
<b>Net Change</b>	\$ (13,374)	\$ (10,471,730)	\$ 0	\$ (10,485,104)
<b>Cumulative Results of Operations</b>	\$ 36,212	\$ 152,616,552	\$ 0	\$ 152,652,764
<b>UNEXPENDED APPROPRIATIONS</b>				
<b>Beginning Balances</b>	\$ 0	\$ 162,359,241	\$ 0	\$ 162,359,241
<b>Beginning balances, as adjusted</b>	\$ 0	\$ 162,359,241	\$ 0	\$ 162,359,241
<b>Budgetary Financing Sources:</b>				
Appropriations received	0	204,348,664	0	204,348,664
Appropriations transferred-in/out	0	1,191,111	0	1,191,111
Other adjustments (rescissions, etc)	0	(8,369,207)	0	(8,369,207)
Appropriations used	0	(212,276,952)	0	(212,276,952)
<b>Total Budgetary Financing Sources</b>	\$ 0	\$ (15,106,384)	\$ 0	\$ (15,106,384)
<b>Unexpended Appropriations</b>	0	147,252,857	0	147,252,857
<b>Net Position</b>	\$ 36,212	\$ 299,869,409	\$ 0	\$ 299,905,621

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.

Department of Defense - Army General Fund

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**As of September 30, 2012 and 2011  
(Amounts in thousands)

	2011 Earmarked Funds	2011 All Other Funds	2011 Eliminations	2011 Consolidated
<b>CUMULATIVE RESULTS OF OPERATIONS</b>				
<b>Beginning Balances</b>	\$ 58,686	\$ 157,181,313	\$ 0	\$ 157,239,999
<b>Beginning balances, as adjusted</b>	\$ 58,686	\$ 157,181,313	\$ 0	\$ 157,239,999
<b>Budgetary Financing Sources:</b>				
Appropriations used	(54)	228,493,138	0	228,493,084
Nonexchange revenue	2,471	0	0	2,471
Donations and forfeitures of cash and cash equivalents	6,719	0	0	6,719
Transfers-in/out without reimbursement	0	700,000	0	700,000
<b>Other budgetary financing sources</b>	0	0	0	0
Donations and forfeitures of property	0	237	0	237
Transfers-in/out without reimbursement (+/-)	(3,641)	1,804,306	0	1,800,665
Imputed financing from costs absorbed by others	0	1,283,044	0	1,283,044
Other (+/-)	810	(10,435,219)	0	(10,434,409)
<b>Total Financing Sources</b>	\$ 6,305	\$ 221,845,506	\$ 0	\$ 221,851,811
<b>Net Cost of Operations (+/-)</b>	15,405	215,938,537	0	215,953,942
<b>Net Change</b>	\$ (9,100)	\$ 5,906,969	\$ 0	\$ 5,897,869
<b>Cumulative Results of Operations</b>	\$ 49,586	\$ 163,088,282	\$ 0	\$ 163,137,868
<b>UNEXPENDED APPROPRIATIONS</b>				
<b>Beginning Balances</b>	\$ 0	\$ 158,281,584	\$ 0	\$ 158,281,584
<b>Beginning balances, as adjusted</b>	\$ 0	\$ 158,281,584	\$ 0	\$ 158,281,584
<b>Budgetary Financing Sources:</b>				
Appropriations received	0	236,165,926	0	236,165,926
Appropriations transferred-in/out	0	772,258	0	772,258
Other adjustments (rescissions, etc)	(54)	(4,367,389)	0	(4,367,443)
Appropriations used	54	(228,493,138)	0	(228,493,084)
<b>Total Budgetary Financing Sources</b>	\$ 0	\$ 4,077,657	\$ 0	\$ 4,077,657
<b>Unexpended Appropriations</b>	0	162,359,241	0	162,359,241
<b>Net Position</b>	\$ 49,586	\$ 325,447,523	\$ 0	\$ 325,497,109

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.

Department of Defense - Army General Fund

**COMBINED STATEMENT OF BUDGETARY RESOURCES**

As of September 30, 2012 and 2011 (Amounts in thousands)

As of September 30, 2012 and 2011 (Amounts in thousands)	2012 Combined		2011 Combined	
<b>BUDGETARY FINANCING ACCOUNTS</b>				
<b>BUDGETARY RESOURCES</b>				
Unobligated balance brought forward, Oct 1	\$	51,648,890	\$	48,310,809
Unobligated balance brought forward, Oct 1, as adjusted	\$	51,648,890	\$	48,310,809
Recoveries of prior year unpaid obligations		34,550,292		24,828,910
Other changes in unobligated balance (+/-)		(3,235,952)		(2,199,068)
Unobligated balance from prior year budget authority, net	\$	82,963,230	\$	70,940,651
Appropriations (discretionary and mandatory)		201,552,120		235,479,831
Spending authority from offsetting collections (discretionary and mandatory)		27,636,567		28,674,059
<b>Total Budgetary Resources</b>	\$	312,151,917	\$	335,094,541
<b>STATUS OF BUDGETARY RESOURCES</b>				
Obligations incurred	\$	267,822,441	\$	283,444,181
Unobligated balance, end of year				
Apportioned		32,503,140		41,866,513
Exempt from apportionment		9,845		4,959
Unapportioned		11,816,491		9,778,888
Total unobligated balance, end of year	\$	44,329,476	\$	51,650,360
<b>Total Budgetary Resources</b>	\$	312,151,917	\$	335,094,541
<b>Change in Obligated Balance</b>				
Unpaid obligations, brought forward, October 1 (gross)	\$	142,457,252	\$	143,921,216
Uncollected customer payments from federal sources, brought forward, October 1 (-)		(27,993,577)		(25,572,774)
Obligated balance start of year (net), before adjustments (+/-)		114,463,675		118,348,442
Obligated balance, start of year (net), as adjusted	\$	114,463,675	\$	118,348,442
Obligations incurred		267,822,441		283,444,181
Outlays (gross) (-)		(236,999,558)		(260,080,898)
Change in uncollected customer payments from federal sources (+/-)		(1,382,844)		(2,420,803)
Recoveries of prior year unpaid obligations (-)		(34,550,292)		(24,828,910)
Subtotal	\$	109,353,422	\$	114,462,012
Obligated balance, end of year				
Unpaid obligations, end of year (gross)		138,729,843		142,455,588
Uncollected customer payments from federal sources, end of year (-)		(29,376,421)		(27,993,577)
<b>Obligated Balance, End of Year</b>	\$	109,353,422	\$	114,462,012
<b>Budget Authority and Outlays, Net</b>				
Budget authority, gross (discretionary and mandatory)	\$	229,188,687	\$	264,153,890
Actual offsetting collections (discretionary and mandatory) (-)		(26,253,722)		(26,253,256)
Change in uncollected customer payments from federal sources (discretionary and mandatory) (+/-)		(1,382,844)		(2,420,803)
Budget authority, net (discretionary and mandatory)	\$	201,552,121	\$	235,479,831
Outlays, gross (discretionary and mandatory)	\$	236,999,558	\$	260,080,898
Actual offsetting collections (discretionary and mandatory) (-)		(26,253,722)		(26,253,256)
Outlays, net (discretionary and mandatory)		210,745,836		233,827,642
Distributed offsetting receipts (-)		828,530		(856,292)
<b>Agency Outlays, Net (Discretionary and Mandatory)</b>	\$	211,574,366	\$	232,971,350

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.

Department of Defense - Army General Fund

**COMBINED STATEMENT OF BUDGETARY RESOURCES**

<i>As of September 30, 2012 and 2011 (Amounts in thousands)</i>	<b>2012 Combined</b>		<b>2011 Combined</b>	
<b>NONBUDGETARY RESOURCES</b>				
Unobligated balance brought forward, Oct 1	\$	275	\$	3,641
Unobligated balance brought forward, Oct 1, as adjusted	\$	275	\$	3,641
Other changes in unobligated balance (+/-)		(1)		0
Unobligated balance from prior year budget authority, net	\$	274	\$	3,641
Spending authority from offsetting collections (discretionary and mandatory)		743		275
<b>Total Budgetary Resources</b>	<b>\$</b>	<b>1,017</b>	<b>\$</b>	<b>3,916</b>
<b>STATUS OF BUDGETARY RESOURCES</b>				
Obligations incurred	\$	0	\$	5,108
Unobligated balance, end of year				
Apportioned		975		51
Unapportioned		42		(1,242)
Total unobligated balance, end of year	\$	1,017	\$	(1,191)
<b>Total Budgetary Resources</b>	<b>\$</b>	<b>1,017</b>	<b>\$</b>	<b>3,917</b>
<b>Change in Obligated Balance</b>				
Uncollected customer payments from federal sources, brought forward, October 1 (-)	\$	(120)	\$	0
Obligated balance start of year (net), before adjustments (+/-)		(120)		0
Obligated balance, start of year (net), as adjusted	\$	(120)	\$	0
Obligations incurred		0		5,108
Outlays (gross) (-)		0		(3,444)
Change in uncollected customer payments from federal sources (+/-)		120		(120)
Subtotal	\$	0	\$	1,544
Obligated balance, end of year				
Unpaid Obligations, end of year (gross)		0		1,664
Uncollected customer payments from federal sources, end of year (-)		0		(120)
<b>Obligated Balance, End of Year</b>	<b>\$</b>	<b>0</b>	<b>\$</b>	<b>1,544</b>
<b>Budget Authority and Outlays, Net</b>				
Budget authority, gross (discretionary and mandatory)	\$	743	\$	275
Actual offsetting collections (discretionary and mandatory) (-)		(863)		(155)
Change in uncollected customer payments from federal sources (discretionary and mandatory) (+/-)		120		(120)
Budget authority, net (discretionary and mandatory)	\$	0	\$	0
Outlays, gross (discretionary and mandatory)	\$	0	\$	3,444
Actual offsetting collections (discretionary and mandatory) (-)		(863)		(155)
Outlays, net (discretionary and mandatory)	\$	(863)	\$	3,289
<b>Agency Outlays, Net (Discretionary and Mandatory)</b>	<b>\$</b>	<b>(863)</b>	<b>\$</b>	<b>3,289</b>

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.



## NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

### 1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Army General Fund (GF), as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the Army GF in accordance with, and to the extent possible, U.S. generally accepted accounting principles (USGAAP) promulgated by the Federal Accounting Standards Advisory Board; the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*; and the *Department of Defense (DoD) Financial Management Regulation*. The accompanying financial statements account for all resources for which the Army GF is responsible unless otherwise noted.

Information relative to classified assets, programs, and operations is excluded from the statements or otherwise aggregated and reported in such a manner that it is not discernible.

The Army GF is unable to fully implement all elements of USGAAP and the OMB Circular No. A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. The Army GF derives reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory and logistics systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with USGAAP.

The Army GF has implemented process and system improvements addressing these limitations to include deployment of the General Fund Enterprise Business System (GFEBS). The GFEBS is a web-based enterprise resource planning system that will help to improve financial performance, standardize business processes, ensure that capability exists to meet future financial management needs, and provide management with relevant, reliable, and timely financial information. The GFEBS will also allow the sharing of standardized and real-time financial, cost, and accounting data across the Army. This system contains the following six major business process areas: funds management; financials; cost management; reimbursement management; spending chain; and property, plant, and equipment.

The Army GF currently has 14 auditor-identified financial statement material weaknesses: (1) Financial Management Systems; (2) Accounting Adjustments; (3) Abnormal Account Balances; (4) Intragovernmental Eliminations; (5) Fund Balance with Treasury; (6) Accounts Receivable; (7) Inventory; (8) General Property, Plant, and Equipment; (9) Accounts Payable; (10) Environmental Liabilities; (11) Statement of Net Cost; (12) Reconciliation of Net Cost of Operations to Budget; (13) Statement of Budgetary Resources; and (14) Contingency Payment Audit Trails.

### 1.B. Mission of the Reporting Entity

The Army mission is to support the national security and defense strategies by providing well-trained, well-led, and well-equipped forces to the combatant commanders. This mission encompasses the intent of the Congress, as defined in Title 10 of the U.S. Code, to preserve the peace and security and provide for the defense of the U.S., its territories, commonwealths, and possessions, and any areas occupied by the U.S.; support national policies; implement national objectives; and overcome any nations responsible for aggressive acts that imperil the peace and security of the U.S.

This mission has been unchanged for the 237-year life of the Army, but the environment and nature of conflict have undergone many changes over that same time, especially with the overseas contingency operations. These contingency operations have required that the Army simultaneously transform the way that it fights, trains, and equips its soldiers. This transformation is progressing rapidly, but it must be taken to its full conclusion if the Army is to continue to meet the nation's domestic and international security obligations today and into the future.

### 1.C. Appropriations and Funds

The Army GF receives appropriations and funds as general, trust, special, and deposit funds. The Army GF uses these appropriations and funds to execute its missions and subsequently report on resource usage.

General funds are used for financial transactions funded by congressional appropriations, including personnel, operation and maintenance, research and development, procurement, and military construction.

These appropriations also include supplemental funds enacted by the American Recovery and Reinvestment Act (Recovery Act) of 2009. Details relating to Recovery Act appropriated funds are available on-line at <http://www.defense.gov/recovery/>.

Trust funds contain receipts and expenditures of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute. Special fund accounts are used to record government receipts reserved for a specific purpose. Certain trust and special funds may be designated as earmarked funds. Earmarked funds are financed by specifically identified revenues; required by statute to be used for designated activities, benefits or purposes; and remain available over time. The Army GF is required to separately account for and report on the receipt, use, and retention of revenues and other financing sources for earmarked funds.

Deposit funds are used to record amounts held temporarily until paid to the appropriate government or public entity. They are not funds of the Army GF and, as such, are not available for the Army GF's operations. The Army GF is acting as an agent or a custodian for funds awaiting distribution.

The Army GF is a party to allocation transfers with other federal agencies as a transferring (parent) entity or receiving (child) entity. An allocation transfer is an entity's legal delegation of authority to obligate budget authority and outlay funds on its behalf. Generally, all financial activity related to allocation transfers (e.g., budget authority, obligations, outlays) is reported in the financial statements of the parent entity. Exceptions to this general rule apply to specific funds for which OMB has directed that all activity be reported in the financial statements of the child entity. These exceptions include U.S. Treasury-Managed Trust Funds, Executive Office of the President (EOP), and all other funds specifically designated by OMB.

The Army GF receives allocation transfers from the Federal Highway Administration and the U.S. Forestry Service. The Army GF receives allocation transfers for the security assistance programs that meet the OMB exception for EOP funds. The activities for these programs are reported separately from the DoD financial statements based on an agreement with OMB.

As a parent, the Army GF allocates funds to the Department of Agriculture and the Department of Transportation for the active Army and Army National Guard.

## 1.D. Basis of Accounting

The Army GF financial management systems are unable to meet all full accrual accounting requirements. Many of the Army GF financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of USGAAP. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by USGAAP. Most of the Army GF financial and nonfinancial legacy systems were designed to record information on a budgetary basis.

The Army GF financial statements and supporting trial balances are compiled from the underlying financial data and trial balances of the Army GF sub-entities. The underlying data is largely derived from budgetary transactions (obligations, disbursements, and collections), from nonfinancial feeder systems, and accruals made for major items such as payroll expenses, accounts payable, and environmental liabilities. Some of the sub-entity level trial balances may reflect known abnormal balances resulting largely from business and system processes. At the consolidated Army GF level, these abnormal balances may not be evident. Disclosures of abnormal balances are made in the applicable footnotes, but only to the extent that the abnormal balances are evident at the consolidated level.

The DoD is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with USGAAP. One such action is the current revision of accounting systems to record transactions based on the United States Standard General Ledger (USSGL). The Army has implemented GFEBS which contains a chart of accounts based on the USSGL. The Army has also created additional subsidiary accounts for GFEBS that track General Fund financial activities at a detailed level. This new system will fully or partially subsume 107 existing systems currently supporting Army GF accounting and financial management, thereby greatly reducing the total number of general ledgers maintained by the Army. However, until all of the Army GF's financial and

nonfinancial feeder systems and processes are updated to collect and report financial information as required by USGAAP, some of the Army GF's financial data will be derived from budgetary transactions, data from nonfinancial feeder systems, and accruals.

### **1.E. Revenues and Other Financing Sources**

The Army GF receives congressional appropriations as financing sources for general funds that expire annually, on a multi-year basis, or do not expire. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The Army GF recognizes revenue as a result of costs incurred for goods and services provided to other federal agencies and the public. Full-cost pricing is the Army GF's standard policy for services provided as required by OMB Circular A-25, *User Charges*. The Army GF recognizes revenue when earned within the constraints of its current system capabilities. In some instances, revenue is recognized when bills are issued.

The Army GF does not include nonmonetary support provided by U.S. allies for common defense and mutual security in amounts reported in the Statement of Net Cost and Note 21, *Reconciliation of Net Cost of Operations to Budget*. The U.S. has cost-sharing agreements with countries having a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in a port.

### **1.F. Recognition of Expenses**

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. Now that GFEBS has been deployed, this system will be the source for the Army GF to derive a substantial portion of its reported data. However, the Army GF is still developing the full functionality of GFEBS and must continue to rely on some current financial and nonfinancial feeder systems that were not designed to collect and record financial information on the full accrual accounting basis. Estimates are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue. In the case of operating materiel and supplies (OM&S), operating expenses are generally recognized when the items are purchased. Efforts are underway to transition to the consumption method for recognizing OM&S expenses. Under the consumption method, OM&S would be expensed when consumed. Due to system limitations, in some instances expenditures for capital and other long-term assets may be recognized as operating expenses. The Army GF continues to implement process and system improvements to address these limitations.

### **1.G. Accounting for Intragovernmental Activities**

Accounting standards require an entity to eliminate intraentity activity and balances from consolidated financial statements in order to prevent an overstatement for business with itself. However, the Army GF cannot accurately identify intragovernmental transactions by customer because the Army GF's systems do not track buyer and seller data at the transaction level. Generally, seller entities within the DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances and are then eliminated. The DoD is implementing replacement systems and a standard financial information structure (SFIS) that will incorporate the necessary elements that will enable DoD to correctly report, reconcile, and eliminate intragovernmental balances. During 4th Quarter, FY 2012, the Army deployed GFEBS, a replacement system, which has incorporated the SFIS chart of accounts.

The Treasury Financial Manual, Part 2 – Chapter 4700, *Agency Reporting Requirements for the Financial Report of the United States Government*, provides guidance for reporting and reconciling intragovernmental balances. While the Army GF is unable to fully reconcile intragovernmental transactions with all federal agencies, the Army GF is able to reconcile balances pertaining to investments in federal securities, Federal Employees' Compensation Act transactions with the Department of Labor, and benefit program transactions with the Office of Personnel Management.

The DoD's proportionate share of public debt and related expenses of the federal government is not included. The federal government does not apportion debt and its related costs to federal agencies. The DoD financial statements do not report any public debt, interest or source of public financing, whether from issuance of debt or tax revenues.

Generally, financing for the construction of DoD facilities is obtained through appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the U.S. Treasury does not allocate such costs to DoD.

## **1.H. Transactions with Foreign Governments and International Organizations**

Each year, the Army GF sells defense articles and services to foreign governments and international organizations under the provisions of the Arms Export Control Act of 1976. Under the provisions of the Act, the DoD has authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the federal government. Payment in U.S. dollars is required in advance.

### **1.I. Funds with the U.S. Treasury**

The Army GF maintains its monetary resources in U.S. Treasury accounts. The disbursing offices of the Defense Finance and Accounting Service (DFAS), Military Departments, and U.S. Army Corps of Engineers (USACE) and the financial service centers of the Department of State process the majority of the worldwide cash collections, disbursements, and adjustments of the Army GF. Each disbursing station prepares monthly reports to the U.S. Treasury on checks issued, electronic fund transfers, interagency transfers, and deposits.

In addition, DFAS sites and USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. On a monthly basis, the Army GF adjusts its FBWT to agree with the U.S. Treasury accounts.

### **1.J. Cash and Other Monetary Assets**

Cash is the total of cash resources under the control of DoD, which includes coin, paper currency, negotiable instruments, and amounts held for deposit in banks and other financial institutions. Foreign currency consists of the total U.S. dollar equivalent of both purchased and nonpurchased foreign currencies held in foreign currency fund accounts. Foreign currency is valued using the U.S. Treasury prevailing rate of exchange.

The majority of cash and all foreign currency is classified as "nonentity" and is restricted. Amounts reported consist primarily of cash and foreign currency held by disbursing officers to carry out their paying, collecting, and foreign currency accommodation exchange missions.

The Army GF conducts a significant portion of operations overseas. The Congress established a special account to handle the gains and losses from foreign currency transactions for five general fund appropriations: (1) operation and maintenance; (2) military personnel; (3) military construction; (4) family housing operation and maintenance; and (5) family housing construction. The gains and losses are calculated as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year. Foreign currency fluctuations related to other appropriations require adjustments to the original obligation amount at the time of payment. The Army GF does not separately identify currency fluctuation transactions.

### **1.K. Accounts Receivable**

Accounts receivable from other federal entities or the public include accounts receivable, claims receivable, and refunds receivable. Generally, allowances for uncollectible accounts due from the public are based upon analysis of collection experience by age category. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual.



## **1.L. Direct Loans and Loan Guarantees**

The Army GF operates the Armament Retooling and Manufacturing Support Initiative under Title 10, United States Code 4551-4555. This loan guarantee program was designed to encourage commercial use of inactive government facilities. The revenue generated from property rental offsets the cost of maintaining these facilities.

The Federal Credit Reform Act of 1990 governs all amended direct loan obligations and loan guarantee commitments made after FY 1991.

## **1.M. Inventories and Related Property**

The Army GF manages only military- or government-specific materiel under normal conditions. Materiel is a unique term that relates to military force management and includes items such as ships, tanks, self-propelled weapons, aircraft and related spares, repair parts, and support equipment. Items commonly used in and available from the commercial sector are not managed in Army GF materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The Army GF holds materiel based on military need and support for contingencies.

Related property includes OM&S and stockpile materiel. The OM&S, including ammunition not held for sale, are valued at standard purchase price. The Army GF uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and are reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, the Army GF uses the purchase method. Under this method, materiel and supplies are expensed when purchased. During FY 2012 and FY 2011, the Army GF expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user. This is a material weakness for the DoD; long-term system corrections are in process. Once the proper systems are in place, ammunition will be accounted for under the consumption method of accounting. All remaining OM&S items will be accounted for under the purchase method because management has deemed these items are in the hands of the end-users.

The Army GF determined that the recurring high-dollar value of OM&S in need of repair is material to the financial statements and requires a separate reporting category. Many high-dollar items, such as aircraft engines, are categorized as OM&S rather than military equipment.

The Army GF recognizes excess, obsolete, and unserviceable OM&S at a net realizable value of \$0 pending development of an effective means of valuing such materiel.

## **1.N. Investments in U.S. Treasury Securities**

The Army GF reports investments in U.S. Treasury securities at cost, net of amortized premiums or discounts. Premiums or discounts are amortized over the term of the investments using the effective interest rate method or another method obtaining similar results. The intent of the Army GF is to hold investments to maturity, unless they are needed to finance claims or otherwise sustain operations. Consequently, a provision is not made for unrealized gains or losses on these securities.

The Army GF invests in nonmarketable market-based U.S. Treasury securities which are issued to federal agencies by the U.S. Treasury Bureau of the Public Debt. They are not traded on any securities exchange but mirror the prices of particular U.S. Treasury securities traded in the government securities market.

## **1.O. General Property, Plant and Equipment**

The Army GF uses the estimated historical cost for valuing military equipment. The DoD identified the universe of military equipment by accumulating information relating to program funding and associated military equipment, equipment useful life, program acquisitions, and disposals to establish a baseline. The military equipment baseline is updated using expenditure, acquisition, and disposal information.

The DoD general property, plant and equipment (PP&E) capitalization threshold is \$100 thousand except for real property, which is \$20 thousand. The Army GF has fully implemented this threshold for real property.

General PP&E assets are capitalized at historical acquisition cost when an asset has a useful life of two or more years and when the acquisition cost equals or exceeds the DoD capitalization threshold. The DoD also requires the capitalization of improvements to existing general PP&E assets if the improvements equal or exceed the capitalization threshold and extend the useful life or increase the size, efficiency, or capacity of the asset. The DoD depreciates all general PP&E, other than land, on a straight-line basis.

When it is in the best interest of the government, the Army GF provides government property to contractors to complete contract work. The Army GF either owns or leases such property, or it is purchased directly by the contractor for the government based on contract terms. When the value of contractor-procured general PP&E meets or exceeds the DoD capitalization threshold, federal accounting standards require that it be reported on the Army GF Balance Sheet.

The DoD developed policy and a reporting process for contractors with government-furnished equipment that provides appropriate general PP&E information for financial statement reporting. The DoD requires Army GF to maintain, in its property systems, information on all property furnished to contractors. These actions are structured to capture and report the information necessary for compliance with federal accounting standards. The Army GF has not fully implemented this policy primarily due to system limitations.

## **1.P. Advances and Prepayments**

When advances are permitted by law, legislative action, or presidential authorization, the DoD policy is to record advances and prepayments in accordance with USGAAP. As such, payments made in advance of the receipt of goods and services should be reported as an asset on the Balance Sheet. The DoD policy is to expense and properly classify assets when the related goods and services are received. The Army GF has not fully implemented the policy for advances identified in contract feeder systems primarily due to system limitations.

## **1.Q. Leases**

Lease payments for the rental of equipment and operating facilities are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease), and the value equals or exceeds the current capitalization threshold, the Army GF records the applicable asset as though purchased, with an offsetting liability, and depreciates it. The Army GF records the asset and liability at (a) the lesser of the present value of the rental and other lease payments during the lease term (excluding portions representing executory costs paid to the lessor) or (b) the fair market value of the asset. The discount rate for the present value calculation is either the lessor's implicit interest rate or the government's incremental borrowing rate at the inception of the lease. The Army GF, as the lessee, receives the use and possession of leased property—for example, real estate or equipment—from a lessor in exchange for a payment of funds. An operating lease does not substantially transfer all the benefits and risk of ownership. Payments for operating leases are expensed over the lease term as they become payable.

Office space and leases entered into by the Army GF are the largest component of operating leases and are based on costs gathered from existing leases, General Services Administration bills, and interservice support agreements. Future-year projections use the Consumer Price Index.

## **1.R. Other Assets**

Other assets include those amounts, such as military and civil service employee pay advances, travel advances, and certain contract financing payments that are not reported elsewhere on the Army GF's Balance Sheet.

The Army GF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, the Army GF may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements to a contractor prior to acceptance of supplies or services by the government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advances and interim

payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. It is DoD policy to record certain contract financing payments as other assets. The Army GF has not fully implemented this policy primarily due to system limitations.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion. The Defense Federal Acquisition Regulation Supplement authorizes progress payments based on a percentage or stage of completion only for construction of real property, shipbuilding and ship conversion, alteration, or repair. Progress payments based on percentage- or stage-of-completion are reported as Construction-in-Progress.

## **1.S. Contingencies and Other Liabilities**

The Statement of Federal Financial Accounting Standards (SFFAS) No. 5, *Accounting for Liabilities of the Federal Government*, as amended by SFFAS No. 12, *Recognition of Contingent Liabilities Arising from Litigation*, defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss. The uncertainty will be resolved when one or more future events occur or fail to occur. The Army GF recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist but there is at least a reasonable possibility of incurring a loss or additional losses. The risk of loss and resultant contingent liabilities for the Army GF arise from pending or threatened litigation or claims and assessments due to events such as aircraft, ship, and vehicle accidents; medical malpractice; property or environmental damages; and contract disputes.

Other liabilities also arise as a result of anticipated disposal costs for Army GF assets. Consistent with SFFAS No. 6, *Accounting for Property, Plant and Equipment*, recognition of an anticipated environmental disposal liability begins when the asset is placed into service. Based on DoD policy, which is consistent with SFFAS No. 5, nonenvironmental disposal liabilities are recognized when management decides to dispose of an asset. The DoD recognizes nonenvironmental disposal liabilities for military equipment nuclear-powered assets when placed into service. These amounts are not easily distinguishable and are developed in conjunction with environmental disposal costs.

## **1.T. Accrued Leave**

The Army GF reports liabilities for military leave and accrued compensatory and annual leave for civilians. Sick leave for civilians is expensed as taken. The liabilities are based on current pay rates.

## **1.U. Net Position**

Net position consists of unexpended appropriations and cumulative results of operations.

Unexpended appropriations represent the amounts of budget authority that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred.

Cumulative results of operations represent the net difference between expenses and losses and financing sources (including appropriations, revenue, and gains) since inception. The cumulative results of operations also include donations and transfers in and out of assets that were not reimbursed.

## **1.V. Treaties for Use of Foreign Bases**

The DoD has the use of the land, buildings, and other overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. The Army GF purchases capital assets overseas with appropriated funds; however, the host country retains title to the land and capital improvements. Treaty terms generally allow the Army GF continued use of these properties until the treaties expire. In the event treaties or other agreements are terminated, use of the foreign bases is prohibited and

losses are recorded for the value of any nonretrievable capital assets. The settlement due to the U.S. or host nation is negotiated and takes into account the value of capital investments and may be offset by the cost of environmental cleanup.

### 1.W. Undistributed Disbursements and Collections

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to specific obligations, payables, or receivables in the source systems and those reported by the U.S. Treasury. Supported disbursements and collections are evidenced by corroborating documentation that would generally support the summary level adjustments made to accounts payable and receivable. Unsupported disbursements and collections do not have supporting documentation for the transactions and most likely would not meet audit scrutiny. However, both supported and unsupported adjustments may have been made to the Army GF accounts payable and receivable trial balances before validating the underlying transactions that established the accounts payable and receivable. As a result, misstatements of reported accounts payable and receivables are likely present in the Army GF financial statements.

Due to noted material weakness in current accounting and financial feeder systems, the DoD is generally unable to determine whether undistributed disbursements and collections should be applied to federal or nonfederal accounts payables and receivable at the time accounting reports are prepared. Accordingly, the DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Both supported and unsupported undistributed disbursements and collections are then applied to reduce accounts payable and receivable accordingly.

### 1.X. Fiduciary Activities

Fiduciary cash and other assets are not assets of the Army GF and are not recognized on the balance sheet. Fiduciary activities are reported on the financial statement note schedules.

### 1.Y. Military Retirement and Other Federal Employment Benefits

Not applicable.

### 1.Z. Significant Events

There were no significant events as of September 30, 2012.

## NOTE 2. NONENTITY ASSETS

As of September 30	2012		2011	
(Amounts in thousands)				
<b>1. Intragovernmental Assets</b>				
A. Fund Balance with Treasury	\$	63,951	\$	175,340
B. Accounts Receivable		0		0
C. Other Assets		0		0
D. Total Intragovernmental Assets	\$	63,951	\$	175,340
<b>2. Nonfederal Assets</b>				
A. Cash and Other Monetary Assets	\$	1,526,881	\$	1,432,966
B. Accounts Receivable		135,533		88,055
C. Other Assets		0		0
D. Total Nonfederal Assets	\$	1,662,414	\$	1,521,021
<b>3. Total Nonentity Assets</b>	\$	1,726,365	\$	1,696,361
<b>4. Total Entity Assets</b>		350,350,331		379,988,515
<b>5. Total Assets</b>	\$	352,076,696	\$	381,684,876



## Information Related to Nonentity Assets

Nonentity assets are assets for which the Army General Fund (GF) maintains stewardship accountability and reporting responsibility. These assets are not available for the Army GF's normal operations.

Nonentity Fund Balance with Treasury consists of deposit funds for humanitarian relief and reconstruction, seized Iraqi cash, and Development Fund Iraq (DFI). Deposit funds are generally used to record amounts held temporarily until paid to the appropriate government or public entity. Humanitarian relief and reconstruction deposit funds are funds held for expenditures on behalf of the Iraqi people. Seized Iraqi cash is former Iraqi regime monies confiscated by coalition forces. The DFI consists of proceeds from Iraqi oil sales, repatriated assets from the United States and other nations, and deposits from unencumbered oil-for-food program funds. The deposit funds for seized Iraqi cash and DFI consist of residual amounts only.

Nonentity Cash and Other Monetary Assets consist of cash held by disbursing officers to carry out their paying and collecting missions. These amounts also include foreign currency accommodation exchange primarily consisting of the burden-sharing for the Republic of Korea. Foreign currency is valued using the U.S. Treasury prevailing rate of exchange.

Nonentity Nonfederal Accounts Receivable are primarily from canceled year appropriations and interest receivables. These receivables will be returned to the U.S. Treasury as miscellaneous receipts once collected.

## NOTE 3. FUND BALANCE WITH TREASURY

As of September 30	2012		2011	
(Amounts in thousands)				
1. Fund Balances				
A. Appropriated Funds	\$	153,169,353	\$	166,762,831
B. Revolving Funds		1,018		155
C. Trust Funds		3,923		1,985
D. Special Funds		30,206		45,001
E. Other Fund Types		63,951		175,340
F. Total Fund Balances	\$	153,268,451	\$	166,985,312
2. Fund Balances Per Treasury Versus Agency				
A. Fund Balance per Treasury	\$	157,077,553	\$	169,770,205
B. Fund Balance per Army		153,268,451		166,985,312
3. Reconciling Amount				
	\$	3,809,102	\$	2,784,893

## Information Related to Fund Balance with Treasury

### Other Fund Types

Other Fund Types consist of deposit funds, clearing accounts, unavailable receipt accounts, seized Iraqi cash, and the Development Fund Iraq (DFI). Deposit funds are generally used to record amounts held temporarily until paid to the appropriate government or public entity. Clearing accounts are used as a temporary suspense account until later paid by or refunded into another account or when the government acts as a banker or agent for others. Unavailable receipt accounts are credited with all collections not earmarked by law for a specific purpose. These collections include taxes, customs duties, and miscellaneous receipts. Seized Iraqi cash is former Iraqi regime monies confiscated by coalition forces. The DFI consists of proceeds from Iraqi oil sales, repatriated assets from the United States and other nations, and deposits from unencumbered oil-for-food program funds.

### Reconciling Amount

The U.S. Treasury reported \$3.8 billion more in Fund Balance with Treasury (FBWT) than reported by the Army General Fund. This difference includes \$3.5 billion in canceling year authority, \$267.6 million in unavailable receipts, \$6.1 million in fiduciary activity, and \$6.3 million in net differences due to the U.S. Treasury treatment of allocation transfers. The allocation transfers reconciling difference results from instances in which Army allocates to or is allocated funds from various governmental entities. In cases in which Army is allocated funds, the amount is excluded from the Fund Balance per Army, but included in Fund Balance per Treasury. In

cases in which Army allocates funds, the amount is included in the Fund Balance per Army, but it is excluded from the Fund Balance per Treasury.

## Status of Fund Balance with Treasury

As of September 30	2012		2011	
(Amounts in thousands)				
1. Unobligated Balance				
A. Available	\$	32,513,961	\$	41,871,522
B. Unavailable		11,816,533		9,777,646
2. Obligated Balance Not Yet Disbursed		138,729,843		142,457,252
3. Nonbudgetary FBWT		(413,330)		875,817
4. NonFBWT Budgetary Accounts		(29,378,556)		(27,996,925)
5. Total	\$	153,268,451	\$	166,985,312

## Status of Fund Balance with Treasury Definitions

The Status of FBWT reflects the budgetary resources to support the FBWT and is a reconciliation between budgetary and proprietary accounts. It primarily consists of unobligated and obligated balances. The balances reflect the budgetary authority remaining for disbursement against current and future obligations.

Unobligated Balance is classified as available or unavailable and represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. The unavailable balance consists primarily of funds temporarily precluded from obligation by law which are invested in U.S. Treasury securities. Certain unobligated balances are restricted for future use and are not apportioned for current use. Unobligated balances for trust fund accounts are restricted for use by the public law that established the funds.

Obligated Balance Not Yet Disbursed represents funds that have been obligated for goods and services not received, and those received but not paid.

Nonbudgetary FBWT includes accounts that do not have budgetary authority, such as deposit funds, unavailable receipt accounts, clearing accounts, nonentity FBWT and Iraqi custodial accounts.

NonFBWT Budgetary Accounts reduce the Status of FBWT. Examples include borrowing authority and investment accounts, accounts receivable, as well as unfilled orders without advance from customers.

## NOTE 4. INVESTMENTS AND RELATED INTEREST

As of September 30	2012				
	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net	Market Value Disclosure
<i>(Amounts in thousands)</i>					
<b>1. Intragovernmental Securities</b>					
A. Nonmarketable, Market-Based					
1. Military Retirement Fund	\$ 0		\$ 0	\$ 0	\$ 0
2. Medicare-Eligible Retiree Health Care Fund	0		0	0	0
3. US Army Corps of Engineers	0		0	0	0
4. Other Funds	2,219	Effective interest	(49)	2,170	2,174
5. Total Nonmarketable, Market-Based	\$ 2,219		\$ (49)	\$ 2,170	\$ 2,174
B. Accrued Interest	11			11	11
C. Total Intragovernmental Securities	\$ 2,230		\$ (49)	\$ 2,181	\$ 2,185
<b>2. Other Investments</b>					
A. Total Other Investments	\$ 0		\$ 0	\$ 0	N/A

**As of September 30***(Amounts in thousands)***1. Intragovernmental Securities****A. Nonmarketable, Market-Based**

	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net	Market Value Disclosure
1. Military Retirement Fund	\$ 0		\$ 0	\$ 0	\$ 0
2. Medicare-Eligible Retiree Health Care Fund	0		0	0	0
3. US Army Corps of Engineers	0		0	0	0
4. Other Funds	3,219	Effective interest	(31)	3,188	3,192
5. Total Nonmarketable, Market-Based	\$ 3,219		\$ (31)	\$ 3,188	\$ 3,192

**B. Accrued Interest**

17	(17)	17
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**C. Total Intragovernmental Securities**

\$ 3,236	\$ (31)	\$ 3,205	\$ 3,209
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**2. Other Investments****A. Total Other Investments**

\$ 0	\$ 0	\$ 0	N/A
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**Information Related to Investments and Related Interest**

Other Funds include the Army Gift Fund. The Army Gift Fund was established to control and account for the disbursement and use of monies donated to the Army General Fund (GF) along with the interest received from the investment of such donations. The related earnings are allocated to the appropriate Army GF activities to be used in accordance with the directions of the donor. These funds are recorded as Nonmarketable Market-Based U.S. Treasury Securities, which are not traded on any securities exchange, but mirror the prices of marketable securities with similar terms.

The U.S. Treasury securities are issued to the earmarked funds as evidence of its receipts and are an asset to the Army GF and a liability to the U.S. Treasury. The federal government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. The cash generated from earmarked funds is deposited in the U.S. Treasury, which uses the cash for general government purposes. Since the Army GF and the U.S. Treasury are both part of the federal government, these assets and liabilities offset each other from the standpoint of the federal government as a whole. For this reason, they do not represent an asset or a liability in the U.S. governmentwide financial statements.

The U.S. Treasury securities provide the Army GF with authority to draw upon the U.S. Treasury to make future benefit payments or other expenditures. When the Army GF requires redemption of these securities to make expenditures, the government will finance them from accumulated cash balances, by raising taxes or other receipts, borrowing from the public, repaying less debt, or curtailing other expenditures. The federal government uses the same method to finance all other expenditures.

On June 1, 2012, the Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards (SFFAS) 43, *Funds from Dedicated Collections*, which amended SFFAS 27, *Identifying and Reporting Earmarked Funds*. The SFFAS 43, which is effective for periods after September 30, 2012, changes the term “earmarked funds” to “funds from dedicated collections” and clarifies the criteria for their classification. In 1st Quarter, FY 2013, the Army GF will assess the gift fund and all other funds currently reported as “earmarked” and report in accordance with SFFAS 43.

**NOTE 5. ACCOUNTS RECEIVABLE****As of September 30***(Amounts in thousands)***1. Intragovernmental Receivables**

	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
1. Intragovernmental Receivables	\$ 353,386	N/A	\$ 353,386
2. Nonfederal Receivables (from the public)	1,486,254	\$ (130,319)	1,355,935
3. Total Accounts Receivable	\$ 1,839,640	\$ (130,319)	\$ 1,709,321

As of September 30 (Amounts in thousands)	2011		
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
1. Intragovernmental Receivables	\$ 538,573	N/A	\$ 538,573
2. Nonfederal Receivables (from the public)	1,055,330	\$ (95,005)	960,325
3. Total Accounts Receivable	\$ 1,593,903	\$ (95,005)	\$ 1,498,898

### Information Related to Accounts Receivable

Accounts Receivable represent the Army General Fund's (GF) claim for payment from other entities. The Army GF only recognizes an allowance for uncollectible amounts from the public. Claims with other federal agencies are resolved in accordance with the Intragovernmental Business Rules.

## NOTE 6. OTHER ASSETS

As of September 30 (Amounts in thousands)	2012	2011
1. Intragovernmental Other Assets		
A. Advances and Prepayments	\$ 434,558	\$ 888,607
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	\$ 434,558	\$ 888,607
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	5,803,153	7,289,438
B. Advances and Prepayments on behalf of Foreign Governments	(1,463,288)	526,135
C. Advances and Prepayments	0	0
D. Total Nonfederal Other Assets	\$ 4,339,865	\$ 7,815,573
3. Total Other Assets	\$ 4,774,423	\$ 8,704,180

### Information Related to Other Assets

Contract terms and conditions for certain types of contract financing payments convey certain rights to the government that protect the contract work from state or local taxation, liens or attachment by the contractor's creditors, transfer of property, or disposition in bankruptcy. However, these rights should not be misconstrued to mean that ownership of the contractor's work has transferred to the federal government. The federal government does not have the right to take the work, except as provided in contract clauses related to termination or acceptance, and the Army General Fund is not obligated to make payment to the contractor until delivery and acceptance.

### Outstanding Contract Financing Payments

The balance of Outstanding Contract Financing Payments includes \$5.3 billion in contract financing payments and an additional \$0.5 billion in estimated future payments to contractors upon delivery and government acceptance of a satisfactory product. Refer to Note 15, *Other Liabilities*, for additional information.

The \$1.5 billion abnormal stems directly from the result of a system change request (SCR). The CFO Load and Reconciliation System was originally implemented and defaulted fiscal years to four alpha characters of RRRR. An SCR implemented in FY 2012 changed this default logic to use actual fiscal years in order to prepare for a future Governmentwide Treasury Account Symbol Adjusted Trial Balance System interface that requires the data to be in valid fiscal years. As a result, this caused proprietary impact in budget execution reporting. These proprietary impacts were corrected in budgetary reporting to cause an in balance effect. This system change coupled with the budget execution adjustments directly attributes to the significant abnormal balance reflected in Advances and Prepayments.



## NOTE 7. CASH AND OTHER MONETARY ASSETS

As of September 30	2012		2011	
(Amounts in thousands)				
1. Cash	\$	194,878	\$	234,302
2. Foreign Currency		1,332,111		1,198,664
3. Other Monetary Assets		0		0
4. Total Cash, Foreign Currency, & Other Monetary Assets	\$	1,526,989	\$	1,432,966

### Information Related to Cash and Other Monetary Assets

Cash consists primarily of cash held by disbursing officers to carry out their paying and collecting mission. Foreign currency consists primarily of burden-sharing funds from the Republic of Korea.

Foreign currency is valued using the U.S. Treasury prevailing rate of exchange. This rate is the most favorable rate that would legally be available to the federal government for foreign currency exchange transactions. The Army General Fund cash and foreign currency are nonentity and are restricted.

## NOTE 8. DIRECT LOAN AND LOAN GUARANTEES

### Direct Loan and/or Loan Guarantee Programs

The Army General Fund (GF) operates a loan guarantee program, the Armament Retooling and Manufacturing Support (ARMS) Initiative Loan Guarantee Program, designed to increase commercial use of inactive government facilities.

The Federal Credit Reform Act of 1990 governs all new and amended direct loan obligations and loan guarantee commitments made after FY 1991. The Army GF does not operate a direct loan program.

Loan guarantee liabilities are reported at the net present value. The cost of the loan guarantee is the net present value of the following estimated projected cash flows: Payments by the Army GF to cover defaults and delinquencies, interest subsidies, or other payments offset by payments to the Army GF including origination and other fees, penalties, and recoveries.

### Armament Retooling and Manufacturing Support Initiative

The Army GF established the ARMS Initiative Loan Guarantee Program, authorized by Title 10, United States Code 4551-4555. The purpose of this program is to encourage commercial use of the Army's inactive ammunition plants through incentives for businesses willing to locate to a government ammunition production facility. The production capacity of these facilities is greater than current military requirements; however, this capacity may be needed by the military in the future. Revenues from property rentals are used to help offset the overhead costs for the operation, maintenance and environmental cleanup at the facilities.

The Army and U.S. Department of Agriculture Rural Business-Cooperative Service (RBS) have established a memorandum of understanding for the RBS to administer this loan guarantee program.

### Loan Guarantees

In an effort to preclude additional Army GF loan liability, the Assistant Secretary of the Army (Acquisition, Logistics and Technology) instituted an ARMS loan guarantee moratorium in 2004. The Army GF continues to operate under the moratorium and does not anticipate initiating new loan guarantees.

**Summary of Direct Loans and Loan Guarantees**

As of September 30	2012		2011	
(Amounts in thousands)				
Loans Receivable				
Direct Loans				
1. Foreign Military Loan Liquidating Account	\$	0	\$	0
2. Military Housing Privatization Initiative		0		0
3. Foreign Military Financing Account		0		0
4. Military Debt Reduction Financing Account		0		0
5. Total Direct Loans	\$	0	\$	0
Defaulted Loan Guarantees				
6. A. Foreign Military Financing Account	\$	0	\$	0
B. Military Housing Privatization Initiative		0		0
C. Armament Retooling & Manufacturing Support Initiative		0		0
7. Total Default Loan Guarantees	\$	0	\$	0
8. Total Loans Receivable	\$	0	\$	0
Loan Guarantee Liability				
1. Foreign Military Liquidating Account	\$	0	\$	0
2. Military Housing Privatization Initiative		0		0
3. Armament Retooling & Manufacturing Support Initiative		1,018		154
4. Total Loan Guarantee Liability	\$	1,018	\$	154

**Information Related to Direct Loans and Loan Guarantees**

The Loan Guarantee Liability represents the present value of the estimated cash inflows less cash outflows of nonacquired loan guarantees. The \$1 million in loan guarantee liability represents the estimated long-term cost of the one remaining performing loan to the U.S. Government for the ARMS Initiative Loan Guarantee Program.

**Direct Loans Obligated**

The Army GF does not operate direct loan programs; therefore, this schedule is not applicable.

**Total Amount of Direct Loans Disbursed**

The Army GF does not operate direct loan programs; therefore, this schedule is not applicable.

**Subsidy Expense for Direct Loan by Program**

The Army GF does not operate direct loan programs; therefore, this schedule is not applicable.

**Subsidy Rate for Direct Loans by Program**

The Army GF does not operate direct loan programs; therefore, this schedule is not applicable.

**Schedule for Reconciling Subsidy Cost Allowance Balances for Post FY1991 Direct Loans**

The Army GF does not operate direct loan programs; therefore, this schedule is not applicable.

## Defaulted Guaranteed Loans

As of September 30	2012		2011	
(Amounts in thousands)				
Defaulted Guaranteed Loans from Pre-FY 1992 Guarantees (Allowance for Loss Method):				
1. Foreign Military Loan Liquidating Account				
A. Defaulted Guaranteed Loans Receivable, Gross	\$	0	\$	0
B. Interest Receivable		0		0
C. Foreclosed Property		0		0
D. Allowance for Loan Losses		0		0
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable, Net	\$	0	\$	0
Defaulted Guaranteed Loans from Post-FY 1991 Guarantees (Present Value Method):				
2. Military Housing Privatization Initiative				
A. Defaulted Guaranteed Loans Receivable, Gross	\$	0	\$	0
B. Interest Receivable		0		0
C. Foreclosed Property		0		0
D. Allowance for Subsidy Cost (Present Value)		0		0
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable, Net	\$	0	\$	0
3. Armament Retooling & Manufacturing Support Initiative				
A. Defaulted Guaranteed Loans Receivable, Gross	\$	735	\$	735
B. Interest Receivable		0		0
C. Foreclosed Property		0		0
D. Allowance for Subsidy Cost (Present Value)		(735)		(735)
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable, Net	\$	0	\$	0
4. Total Value of Assets Related to Defaulted Guaranteed Loans Receivable				
	\$	0	\$	0

## Guaranteed Loans Outstanding

As of September 30		2012		2011	
(Amounts in thousands)		Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed	Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
<b>Guaranteed Loans Outstanding</b>					
1.	Military Housing Privatization Initiative	\$	0	\$	0
2.	Armament Retooling & Manufacturing Support Initiative		0	2,437	2,072
3.	Foreign Military Liquidating Account		0	0	0
<b>4. Total</b>		<b>\$</b>	<b>0</b>	<b>\$</b>	<b>2,437</b>
<b>New Guaranteed Loans Disbursed</b>					
1.	Military Housing Privatization Initiative	\$	0	\$	0
2.	Armament Retooling & Manufacturing Support Initiative		0	0	0
<b>3. Total</b>		<b>\$</b>	<b>0</b>	<b>\$</b>	<b>0</b>

### Information Related to Guaranteed Loans Outstanding Definition

The Outstanding Principal of Guaranteed Loans, Face Value is the principal amount of loans disbursed by third parties and guaranteed by the Army GF. The face value does not include any interest that is due to be paid on the debt instruments.

The Amount of Outstanding Principal Guaranteed is the principal amount of loans disbursed by third parties and guaranteed by the Army GF less borrower collateral. The net amount represents the loan amount guaranteed by the Army GF. One performing loan remains.

## Liabilities for Loan Guarantees

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
<b>Liabilities for Losses on Loan Guarantee from Pre 1992</b>		
<b>(Allowance for Loss):</b>		
1. Foreign Military Liquidating Account	\$ 0	\$ 0
<b>2. Total Loan Guarantee Liability (Pre-FY 1992)</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Liabilities for Loan Guarantee from Post 1991 (Present Value):</b>		
3. Military Housing Privatization Initiative	\$ 0	\$ 0
4. Armament Retooling & Manufacturing Support Initiative	1,018	154
<b>5. Total Loan Guarantee Liability (Post-FY 1991)</b>	<b>\$ 1,018</b>	<b>\$ 154</b>
<b>6. Total Loan Guarantee Liability</b>	<b>\$ 1,018</b>	<b>\$ 154</b>

### Information Related to Liabilities for Loan Guarantees

Liabilities for Loan Guarantee Programs Post-FY 1991 represent the present value of the estimated cash inflows less cash outflows of non-acquired loan guarantees. The \$1 million in loan guarantee liability represents the estimated long-term cost of the currently performing loan to the U. S. Government for the ARMS Initiative Loan Guarantee Program.

## Subsidy Expense for Loan Guarantees by Program

As of September 30

*(Amounts in thousands)*

(Amounts in thousands)

2012	Interest Differential	Defaults	Fees	Other	Total
<b>1. New Loan Guarantees Disbursed:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	0	0	0	0
<b>Totals</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
2011	Interest Differential	Defaults	Fees	Other	Total
<b>2. New Loan Guarantees Disbursed:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	0	0	0	0
<b>Totals</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
2012	Interest Differential	Defaults	Fees	Other	Total
<b>3. Modifications and Reestimates:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	820	0	820	820
<b>Totals</b>	<b>\$ 0</b>	<b>\$ 820</b>	<b>\$ 0</b>	<b>\$ 820</b>	<b>\$ 820</b>
2011	Interest Differential	Defaults	Fees	Other	Total
<b>4. Modifications and Reestimates:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	1	(3,641)	(3,640)	(3,640)
<b>Totals</b>	<b>\$ 0</b>	<b>\$ 1</b>	<b>\$ (3,641)</b>	<b>\$ (3,640)</b>	<b>\$ (3,640)</b>
<b>2012</b>		<b>2011</b>			
<b>5. Total Loan Guarantee:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0			
Armament Retooling & Manufacturing Support Initiative	820	(3,640)			
<b>Totals</b>	<b>\$ 820</b>	<b>\$ (3,640)</b>			

### Information Related to Subsidy Expense for Loan Guarantees by Program

In an effort to preclude additional Army GF loan liability, the Assistant Secretary of the Army (Acquisition, Logistics, and Technology) instituted an ARMS loan guarantee moratorium in 2004. The Army GF continues to operate under the moratorium, and does not anticipate initiating new loan guarantees.

## Subsidy Rates for Loan Guarantees by Program

As of September 30

(Amounts in thousands)

	Interest Supplements	Defaults	Fees and other Collections	Other	Total
<b>Budget Subsidy Rates for Loan Guarantees:</b>					
1. Military Housing Privatization Initiative	0.00%	0.00%	0.00%	0.00%	0.00%
2. Armament Retooling & Manufacturing Support Initiative	0.00%	0.00%	0.00%	0.00%	0.00%

### Information Related to Subsidy Rates for Loan Guarantees by Program

The Subsidy Rates for Loan Guarantees by program table displays subsidy rates applied to new guaranteed loans. Since there have been no new loan guarantees originated since 2004 for the ARMS Initiative Program, the table properly presents zero percent subsidy rates.

## Schedule for Reconciling Loan Guarantee Liability Balances for Post-FY 1991 Loan Guarantees

As of September 30	2012		2011	
(Amounts in thousands)				
Beginning Balance, Changes, and Ending Balance:				
1. Beginning Balance of the Loan Guarantee Liability	\$	154	\$	3,640
2. Add: Subsidy Expense for Guaranteed Loans Disbursed during the Reporting Years by Component				
A. Interest Supplement Costs	\$	0	\$	0
B. Default Costs (Net of Recoveries)		0		0
C. Fees and Other Collections		0		0
D. Other Subsidy Costs		0		0
E. Total of the above Subsidy Expense Components	\$	0	\$	0
3. Adjustments				
A. Loan Guarantee Modifications	\$	0	\$	0
B. Fees Received		0		0
C. Interest Supplements Paid		0		0
D. Foreclosed Property and Loans Acquired		0		0
E. Claim Payments to Lenders		0		0
F. Interest Accumulation on the Liability Balance		44		154
G. Other		0		0
H. Total of the above Adjustments	\$	44	\$	154
4. Ending Balance of the Loan Guarantee Liability before Reestimates		198		3,794
5. Add or Subtract Subsidy Reestimates by Component				
A. Interest Rate Reestimate	\$	820	\$	1
B. Technical/Default Reestimate		0		(3,641)
C. Total of the above Reestimate Components	\$	820	\$	(3,640)
6. Ending Balance of the Loan Guarantee Liability	\$	1,018	\$	154

## Administrative Expenses

Administrative expense for the ARMS Initiative represents \$4,000 per annum for salaries.

## NOTE 9. INVENTORY AND RELATED PROPERTY

As of September 30	2012		2011	
(Amounts in thousands)				
1. Inventory, Net	\$	0	\$	0
2. Operating Materiel & Supplies, Net		30,824,075		31,180,416
3. Stockpile Materiel, Net		0		0
4. Total	\$	30,824,075	\$	31,180,416



## Inventory, Net

Not applicable.

## Operating Materiel and Supplies, Net

As of September 30

(Amounts in thousands)

### 1. OM&S Categories

	OM&S Gross Value	Revaluation Allowance	OM&S, Net	Valuation Method
A. Held for Use	\$ 28,157,681	\$ 0	\$ 28,157,681	SP, LAC, MAC
B. Held for Repair	2,666,394	0	2,666,394	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	235,838	(235,838)	0	NRV
<b>D. Totals</b>	<b>\$ 31,059,913</b>	<b>\$ (235,838)</b>	<b>\$ 30,824,075</b>	

As of September 30

(Amounts in thousands)

### 1. OM&S Categories

	OM&S Gross Value	Revaluation Allowance	OM&S, Net	Valuation Method
A. Held for Use	\$ 31,180,416	\$ 0	\$ 31,180,416	SP, LAC, MAC
B. Held for Repair	0	0	0	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	509,798	(509,798)	0	NRV
<b>D. Totals</b>	<b>\$ 31,690,214</b>	<b>\$ (509,798)</b>	<b>\$ 31,180,416</b>	

#### Legend for Valuation Methods:

LAC = Latest Acquisition Cost  
 SP = Standard Price  
 AC = Actual Cost  
 MAC = Moving Average Cost

NRV = Net Realizable Value  
 LCM = Lower of Cost or Market  
 O = Other

## Information Related to Operating Materiel and Supplies, Net

Operating Materiel and Supplies (OM&S) include ammunition, tactical missiles, and their related spare and repair parts. The Held for Use category, which includes all materiel available to be issued, consists of \$26.1 billion in Held for Use and \$2.1 billion in Held in Reserve for Future Use. Economically repairable materiel is categorized as "Held for Repair."

Managers determine which items are more costly to repair than to replace. The value of these items is offset by an allowance for excess, obsolete, and unserviceable OM&S which results in a net value of zero. The Army General Fund (GF) established this allowance at 100 percent of the carrying account in accordance with DoD policy. These items, which include ammunition and missiles, are reported as Excess, Obsolete, and Unserviceable.

The values of the Army's government-furnished materiel and contractor-acquired materiel in the hands of the contractors are normally not included in the OM&S values reported above. The DoD is presently reviewing its process for reporting these amounts in an effort to determine the appropriate accounting treatment and the best method to collect and report required information annually without duplicating information in other existing logistics systems.

As a result of audit readiness efforts, the Army GF can now identify the Held for Repair portion of OM&S. This breakout was not available in previous years.

Currently, there are no restrictions on OM&S.

## Stockpile Materiel, Net

Not applicable.

## NOTE 10. GENERAL PP&E, NET

As of September 30	2012				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
<i>(Amounts in thousands)</i>					
<b>1. Major Asset Classes</b>					
A. Land	N/A	N/A	\$ 601,132	N/A	\$ 601,132
B. Buildings, Structures, and Facilities	S/L	20 or 40	76,635,801	\$ (30,951,060)	45,684,741
C. Leasehold Improvements	S/L	lease term	36,037	(22,372)	13,665
D. Software	S/L	2-5 or 10	513,887	(216,260)	297,627
E. General Equipment	S/L	5 or 10	20,153,493	(9,082,154)	11,071,339
F. Military Equipment	S/L	various	156,028,694	(63,652,323)	92,376,371
G. Shipbuilding	N/A	N/A	0	0	0
H. Assets Under Capital Lease	S/L	lease term	166,617	(165,747)	870
I. Construction-in-Progress	N/A	N/A	9,925,511	N/A	9,925,511
J. Other			231	(231)	0
<b>K. Total General PP&amp;E</b>			<b>\$ 264,061,403</b>	<b>\$ (104,090,147)</b>	<b>\$ 159,971,256</b>

As of September 30	2011				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
<i>(Amounts in thousands)</i>					
<b>1. Major Asset Classes</b>					
A. Land	N/A	N/A	\$ 519,901	N/A	\$ 519,901
B. Buildings, Structures, and Facilities	S/L	20 or 40	72,230,406	\$ (35,284,447)	36,945,959
C. Leasehold Improvements	S/L	lease term	30,655	(20,606)	10,049
D. Software	S/L	2-5 or 10	501,823	(207,870)	293,953
E. General Equipment	S/L	5 or 10	9,649,888	(4,512,849)	5,137,039
F. Military Equipment	S/L	various	172,188,793	(55,126,843)	117,061,950
G. Shipbuilding	N/A	N/A	0	0	0
H. Assets Under Capital Lease	S/L	lease term	166,617	(164,637)	1,980
I. Construction-in-Progress	N/A	N/A	11,909,068	N/A	11,909,068
J. Other			0	0	0
<b>K. Total General PP&amp;E</b>			<b>\$ 267,197,151</b>	<b>\$ (95,317,252)</b>	<b>\$ 171,879,899</b>

### Legend for Valuation Methods:

S/L = Straight Line      N/A = Not Applicable

### Information Related to General Property, Plant and Equipment

The Army General Fund (GF) uses the estimated historical cost for valuing capital equipment. In 4th Quarter, FY 2012, the Army GF transitioned from using data calls for financial reporting of the following asset classes: land; buildings, structures, and facilities; general equipment; and military equipment. Instead, the General Fund Enterprise Business System populates financial values based on source records in the relevant accountable property system of record. This transition supports Army audit readiness objectives and complies with DoD regulations.

The Army GF is not aware of any restrictions on the use or convertibility of general property, plant, and equipment.

Significant accounting adjustments have been made to the Army GF's mission critical assets as a result of the Department's ongoing audit readiness efforts. These accounting adjustments were recognized in current year gain or loss accounts when auditable data were not available to support restatement of prior-period financial statements.

## Heritage Assets and Stewardship Land Information

The mission of the Army is to provide the military forces needed to deter war and protect the security of the United States by organizing, training, supplying, equipping, and mobilizing forces for assignment in support of that mission. Executing this mission requires efficient and effective use of resources in a manner that ensures operational and environmental sustainability, while respecting the history and heritage that reflect and support the military mission. The Army has stewardship responsibilities for heritage assets that date not only from the military history of the land, but also from prior historic occupations. The Army relies upon heritage assets, such as historic buildings and stewardship land, for daily use in administering, housing, and training soldiers. Heritage assets not currently employed as multi-use, such as archeological collections or museum collections, are items that embody the multi-faceted history of the land, the military, the local communities, and the nation. In that mission, the Army GF, with minor exceptions, uses most of the buildings and stewardship land in its daily activities and includes the buildings on the Balance Sheet as multi-use heritage assets (capitalized and depreciated).

The Statement of Federal Financial Accounting Standards No. 29, *Heritage Assets and Stewardship Land*, issued by the Federal Accounting Standards Advisory Board, requires note disclosures for these types of assets. The Army GF's policy is to preserve its heritage assets, which are items of historical, cultural, educational, or artistic importance.

Heritage assets within the Army GF consist of buildings and structures, archeological sites, and museum collections. The Army GF defines these assets as follows:

### Buildings and Structures

Buildings and structures which are listed on, or eligible for listing on, the National Register of Historic Places, including multi-use heritage assets.

### Archeological Sites

Sites that have been identified, evaluated, and determined to be eligible for, or are listed on, the National Register of Historic Places in accordance with Section 110, National Historical Preservation Act.

### Museum Collection Items

Items which are unique for one or more of the following reasons: historical or natural significance; cultural, educational, or artistic importance; or significant technical or architectural characteristics.

The heritage assets for the Army GF are listed below:

Categories	Measure Quantity	Beginning Balance	Additions	Deletions	Ending Balance
Buildings and Structures	Each	39,681	667	1,678	38,670
Archeological Sites	Each	9,069	398	1,344	8,123
Museum Collection Items (objects, not including fine art)	Each	580,263	6,725	1,019	585,969
Museum Collection Items (objects, fine art)	Each	0	0	0	0

Stewardship land is land and land rights owned by the Department of the Army (DA), but not acquired as, or in connection with, items of General Property, Plant, and Equipment. All land provided to the DA from the public domain or at no cost, regardless of its use, is classified as Stewardship Land.

Stewardship land is presented in context of all categories of DoD lands and reported in acres based on the predominant use of the land. The three categories of Stewardship land held in public trust are as follows: State-Owned Land, Withdrawn Public Land, and Public Land. The DA's stewardship land consists mainly of mission-essential land.

The following is a description of the methods of acquisition and withdrawal of stewardship land:

- Acquiring additional land through donation or withdrawals from public domain.
- Identifying missing land records.
- Disposing of Base Realignment and Closure (BRAC) sites or transferring land to another DoD agency.
- Identifying cemeteries and historical facilities.
- Disposing of BRAC property or excess installations.
- Privatizing residential community initiatives programs.

The Army GF holds the following acres of stewardship land:

(Acres in thousands)

Facility Code	Facility Title	Beginning Balance	Additions <sup>1</sup>	Deletions	Ending Balance
9110	Government-Owned Land	4,931	93	43	4,981
9111	State-Owned Land	7	0	2	5
9120	Withdrawn Public Land	6,446	0	41	6,405
9130	Licensed and Permitted Land	2,093	0	1,906	187
9140	Public Land	11	0	0	11
9210	Land Easement	216	3	1	218
9220	In-leased Land	133	0	112	21
9230	Foreign Land	158	0	157	1
Grand Total					11,829
Total - All Other Land					5,408
Total - Stewardship Land					6,421

Note 1: There were no donations included in the Additions column above.

## Assets Under Capital Lease

As of September 30	2012	2011
(Amounts in thousands)		
<b>1. Entity as Lessee, Assets Under Capital Lease</b>		
A. Land and Buildings	\$ 166,071	\$ 166,071
B. Equipment	546	546
C. Accumulated Amortization	(165,747)	(164,637)
D. Total Capital Leases	\$ 870	\$ 1,980

## NOTE 11. LIABILITIES NOT COVERED BY BUDGETARY RESOURCES

As of September 30	2012	2011
(Amounts in thousands)		
<b>1. Intragovernmental Liabilities</b>		
A. Accounts Payable	\$ 0	\$ 0
B. Debt	0	0
C. Other	504,714	553,337
D. Total Intragovernmental Liabilities	\$ 504,714	\$ 553,337
<b>2. Nonfederal Liabilities</b>		
A. Accounts Payable	\$ 217,902	\$ 170,964
B. Military Retirement and Other Federal Employment Benefits	1,406,105	1,356,264
C. Environmental Liabilities	26,886,368	28,558,194
D. Other Liabilities	6,423,138	7,643,785
E. Total Nonfederal Liabilities	\$ 34,933,513	\$ 37,729,207
<b>3. Total Liabilities Not Covered by Budgetary Resources</b>	\$ 35,438,227	\$ 38,282,544
<b>4. Total Liabilities Covered by Budgetary Resources</b>	16,732,848	17,905,223
<b>5. Total Liabilities</b>	\$ 52,171,075	\$ 56,187,767

### Information Related to Liabilities Not Covered by Budgetary Resources

Liabilities not covered by budgetary resources include liabilities for which congressional action is needed before budgetary resources can be provided.

Intragovernmental Liabilities, Other, consist of Federal Employees' Compensation Act (FECA) and other unfunded employment-related liabilities.

Nonfederal Accounts Payable not covered by budgetary resources represent amounts that are related to canceled appropriations. These amounts will require resources funded from future-year appropriations.

Military Retirement and Other Federal Employment Benefits consist of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities consist primarily of the FECA benefits liability of \$1.4 billion. Refer to Note 17, *Military Retirement and Other Federal Employment Benefits*, for additional details and disclosures.

Environmental Liabilities represent the Department of the Army's liability for existing and anticipated environmental cleanup and disposal.

Nonfederal Other Liabilities primarily consist of \$3.2 billion in unfunded annual leave, \$1.1 billion in contingent liabilities, and \$2.1 billion in expected expenditures for disposal of conventional munitions.

Liabilities such as Environmental Liabilities and Military Retirement and Other Federal Employment Benefits are not covered by budgetary resources because there are no current or immediate appropriations available for liquidation. These liabilities will require resources funded from future-year appropriations.

## NOTE 12. ACCOUNTS PAYABLE

As of September 30 (Amounts in thousands)	2012		
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total
1. Intragovernmental Payables	\$ 1,766,162	N/A	\$ 1,766,162
2. Nonfederal Payables (to the public)	3,183,094	\$ (6,342)	3,176,752
<b>3. Totals</b>	<b>\$ 4,949,256</b>	<b>\$ (6,342)</b>	<b>\$ 4,942,914</b>

As of September 30 (Amounts in thousands)	2011		
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total
1. Intragovernmental Payables	\$ 2,028,077	N/A	\$ 2,028,077
2. Nonfederal Payables (to the public)	6,631,107	\$ 1,457	6,632,564
<b>3. Totals</b>	<b>\$ 8,659,184</b>	<b>\$ 1,457</b>	<b>\$ 8,660,641</b>

### Information Related to Accounts Payable

Accounts Payable include amounts owed to federal and nonfederal entities for goods and services received by the Army General Fund (GF). The Army GF systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side accounts payable are adjusted to agree with intraagency seller-side accounts receivable. Accounts Payable were adjusted by reclassifying amounts between federal and nonfederal Accounts Payable and applying both supported and unsupported undistributed disbursements at the reporting entity level.

## NOTE 13. DEBT

As of September 30 (Amounts in thousands)	2012			2011		
	Beginning Balance	Net Borrowing	Ending Balance	Beginning Balance	Net Borrowing	Ending Balance
<b>1. Agency Debt (Intragovernmental)</b>						
A. Debt to the Treasury	\$ 1	\$ (1)	\$ 0	\$ 1	\$ 0	\$ 1
B. Debt to the Federal Financing Bank	0	0	0	0	0	0
C. Total Agency Debt	\$ 1	\$ (1)	\$ 0	\$ 1	\$ 0	\$ 1
<b>2. Total Debt</b>	<b>\$ 1</b>	<b>\$ (1)</b>	<b>\$ 0</b>	<b>\$ 1</b>	<b>\$ 0</b>	<b>\$ 1</b>



## Information Related to Debt

The Army General Fund (GF), by means of the Armament Retooling and Manufacturing Support (ARMS)-initiative legislation, established a loan guarantee program to facilitate commercial firms' use of specified ammunition manufacturing facilities. When a borrower defaults on a guaranteed loan, the Army GF executes borrowing authority with the U.S. Treasury to pay the lender the guaranteed outstanding principal resulting in a debt with the U.S. Treasury. The total debt of only \$40 consists of interest and principal payments due to the U.S. Treasury for ARMS loan defaults.

## NOTE 14. ENVIRONMENTAL LIABILITIES AND DISPOSAL LIABILITIES

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
<b>1. Environmental Liabilities - Nonfederal</b>		
A. Accrued Environmental Restoration Liabilities		
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	\$ 2,437,261	\$ 2,036,524
2. Active Installations—Military Munitions Response Program (MMRP)	1,419,268	1,869,956
3. Formerly Used Defense Sites—IRP and BD/DR	3,063,392	3,295,377
4. Formerly Used Defense Sites—MMRP	10,842,520	10,990,009
B. Other Accrued Environmental Liabilities—Non-BRAC		
1. Environmental Corrective Action	510,690	326,128
2. Environmental Closure Requirements	206,471	354,103
3. Environmental Response at Operational Ranges	75,878	74,732
4. Asbestos	243,450	246,744
5. Non-Military Equipment	0	0
6. Other	60,146	60,887
C. Base Realignment and Closure Installations		
1. Installation Restoration Program	658,562	673,582
2. Military Munitions Response Program	535,157	530,682
3. Environmental Corrective Action/Closure Requirements	134,225	206,853
4. Asbestos	0	0
5. Non-Military Equipment	0	0
6. Other	0	0
D. Environmental Disposal for Military Equipment/Weapons Programs		
1. Nuclear Powered Military Equipment/Spent Nuclear Fuel	0	0
2. Non-Nuclear Powered Military Equipment	0	0
3. Other Weapons Systems	0	0
E. Chemical Weapons Disposal Program		
1. Chemical Demilitarization - Chemical Materials Agency (CMA)	3,691,127	4,592,023
2. Chemical Demilitarization - Assembled Chemical Weapons Alternatives (ACWA)	6,539,062	6,510,391
3. Other	0	0
<b>2. Total Environmental Liabilities</b>	<b>\$ 30,417,209</b>	<b>\$ 31,767,991</b>

## Information Related to Environmental and Disposal Liabilities

### Applicable Laws and Regulations

The Army General Fund (GF) is required to clean up contamination resulting from past waste disposal practices, leaks, spills, and other past activity. This cleanup requirement applies to releases of hazardous substances and wastes that created a public health

or environmental risk and from unexploded ordnance, discarded military munitions, and munitions constituents at other than operational ranges. The Defense Environmental Restoration Program (DERP), established by Section 211 of the Superfund Amendments and Reauthorization Act of 1986 and codified in Title 10 of the United States Code (USC) 2700 et seq., establishes requirements. The Army GF is also required to clean up contamination resulting from waste disposal practices, leaks, spills, and other activity at overseas locations in accordance with DoD policy as prescribed in DoD Instruction 4715.8, *Environmental Remediation for DoD Activities Overseas, under the Army Compliance Cleanup Program*.

The Federal Accounting Standards Advisory Board (FASAB) published Technical Bulletin 2006-1 (TB 2006-1), *Recognition and Measurement of Asbestos-Related Cleanup Cost*, and Technical Release 10, *Implementation Guidance on Asbestos Cleanup Costs Associated with Facilities and Installed Equipment*, which clarify reporting of liabilities arising from asbestos-related cleanup.

The Army GF is required to destroy the chemical stockpile and nonstockpile items as part of the Chemical Demilitarization Program. The 1986 Defense Authorization Act (Public Law (PL) 99-145, as amended by subsequent acts), directed the DoD to destroy the unitary chemical stockpile while providing for maximum protection of the environment, public, and personnel involved in the destruction effort. The U.S. Army Chemical Materials Agency's Nonstockpile Chemical Materiel Project provides centralized management and direction to the DoD for the disposal of currently declared nonstockpile chemical materiel in a safe and environmentally sound manner. The facilities and equipment developed and fielded as part of the program are also subject to numerous federal and state environmental regulations.

For the environmental liability associated with the destruction of chemical weapons, the schedules and cost estimates in the approved baseline are based on the best information available and have been through the formal acquisition program baseline-approval process at the time of report submission. However, these schedules and estimates are subject to modifications and impacts from program risks and uncertainties inherent to the task of chemical demilitarization and the political sensitivity of the program. These risks may include processing changes required to meet the operational schedules due to the deteriorating condition of the stockpile and additional schedule time and/or cost to address changes in environmental laws or congressional requirements.

Applicable laws are as follows for the DERP, NonDERP, low-level radioactive waste, and the Base Realignment and Closure (BRAC) programs:

- Comprehensive Environmental Response, Compensation, and Liability Act
- Superfund Amendments and Reauthorization Act
- Clean Water Act
- Safe Drinking Water Act
- Clean Air Act
- Resource Conservation and Recovery Act
- Toxic Substances Control Act
- Medical Waste Tracking Act
- Atomic Energy Act
- Low-Level Radioactive Waste Policy Amendments Act
- Nuclear Waste Policy Act
- National Defense Authorization Acts

### **Types of Environmental Liabilities and Disposal Liabilities Identified**

The Army GF has cleanup requirements for DERP sites at active installations, BRAC installations, formerly used Defense sites at active installations that are not covered by DERP, weapon systems programs, and chemical weapons disposal programs. Environmental disposal for weapons systems programs consists of chemical weapons disposal, including the destruction of the entire United States' stockpile of chemical agents and munitions and disposal of nonstockpile chemical material. This includes binary chemical weapons, old chemical weapons recovered as part of remediation and recovery operations, and miscellaneous materiel associated with chemical weapon production, storage, testing, maintenance, and disposal. All cleanup is done in coordination with regulatory agencies, other responsible parties, and current property owners.

**Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods**

The Army GF uses engineering estimates and independently validated models to estimate environmental cleanup liabilities. The Remedial Action Cost Engineering and Requirements (RACER) system is the Army's preferred model. The Army GF relies upon the Air Force, the RACER executive agent, to validate the model in accordance with DoD Instruction 5000.61, *DoD Modeling and Simulation (M&S) Verification, Valuation, and Accreditation (VV&A)*, and primarily uses the model to estimate the liabilities based on data received during a preliminary assessment and initial site investigation. The Army primarily uses engineering estimates after obtaining extensive data during the remedial investigation/feasibility phase of an environmental cleanup project.

The Army GF uses the real property inventory and engineering estimates of costs for environmental closure liabilities and reports these costs in aggregate. Asbestos disposal costs are not estimable due to the ubiquitous nature of non-friable asbestos, but facility surveys to determine the presence of asbestos are reported, based upon a cost of \$0.35 per square foot multiplied by the gross square feet of the Army-owned buildings.

The Army GF is unable to systematically gather and report environmental disposal liabilities for military equipment or general property, plant, and equipment. Most liabilities for individual items of equipment are expected to be below the Army's \$42,000 materiality threshold for a single environmental site. The Army GF will continue to coordinate with the Office of the Under Secretary of Defense (Comptroller) to address this deficiency.

**Nature of Estimates and the Disclosure of Information Regarding Possible Changes Due to Inflation, Deflation, Technology, or Applicable Laws and Regulations**

The Army GF had changes in estimates resulting from (1) previously unknown contamination, (2) better site characterization with sampling information, (3) reestimation based on different assumptions, and (4) lessons learned. Environmental liabilities may change in the future due to changes in laws and regulations, changes in agreements with regulatory agencies, and advances in technology.

**Uncertainty Regarding the Accounting Estimates Used to Calculate the Reported Environmental Liabilities**

The environmental liabilities for the Army GF are based on accounting estimates, which require certain judgments and assumptions that are believed to be reasonable based upon information available at the time the estimates are calculated. The actual results may vary materially from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. Liabilities can be further impacted if investigation of the environmental sites discloses contamination levels different than known at the time of the estimates.

The Army GF has reported asbestos survey costs but estimating the amount of non-friable asbestos removal and disposal at the time of building renovation or demolition, in accordance with FASAB TB 2006-1, presents too much uncertainty to recognize on the Balance Sheet.

The Army GF is also uncertain regarding the costs for remediation activities in conjunction with returning overseas military facilities to host nations. The Army GF is currently unable to provide a reasonable estimate because the extent of remediation required is not known.

Other Accrued Environmental Liabilities – Non-BRAC, Other consists of low-level radioactive waste.

## NOTE 15. OTHER LIABILITIES

As of September 30 (Amounts in thousands)	2012			2011
	Current Liability	Noncurrent Liability	Total	Total
<b>1. Intragovernmental</b>				
A. Advances from Others	\$ 11,539	\$ 0	\$ 11,539	\$ 45,118
B. Deposit Funds and Suspense Account Liabilities	(477,763)	0	(477,763)	832,516
C. Disbursing Officer Cash	1,530,523	0	1,530,523	1,438,076
D. Judgment Fund Liabilities	3,984	0	3,984	20,953
E. FECA Reimbursement to the Department of Labor	117,686	132,822	250,508	252,478
F. Custodial Liabilities	126,325	5,566	131,891	82,946
G. Employer Contribution and Payroll Taxes Payable	152,661	0	152,661	145,608
H. Other Liabilities	267,594	0	267,594	292,213
I. Total Intragovernmental Other Liabilities	\$ 1,732,549	\$ 138,388	\$ 1,870,937	\$ 3,109,908
<b>2. Nonfederal</b>				
A. Accrued Funded Payroll and Benefits	\$ 3,117,091	\$ 0	\$ 3,117,091	\$ 791,599
B. Advances from Others	1,815,150	0	1,815,150	1,804,354
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	65,061	0	65,061	44,072
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Non-nuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	2,136,649	2,136,649	2,752,431
G. Accrued Unfunded Annual Leave	3,939,285	0	3,939,285	3,707,090
H. Capital Lease Liability	1,365	131	1,496	3,453
I. Contract Holdbacks	674,616	0	674,616	488,556
J. Employer Contribution and Payroll Taxes Payable	154,593	0	154,593	(7,515)
K. Contingent Liabilities	51,716	1,577,235	1,628,951	1,707,572
L. Other Liabilities	0	0	0	1,196
M. Total Nonfederal Other Liabilities	\$ 9,818,877	\$ 3,714,015	\$ 13,532,892	\$ 11,292,808
<b>3. Total Other Liabilities</b>	<b>\$ 11,551,426</b>	<b>\$ 3,852,403</b>	<b>\$ 15,403,829</b>	<b>\$ 14,402,716</b>

### Capital Lease Liability

As of September 30 (Amounts in thousands)	2012				2011
	Land and Buildings	Equipment	Other	Total	Total
<b>1. Future Payments Due</b>					
A. 2012	\$ 0	\$ 0	\$ 0	\$ 0	\$ 2,413
B. 2013	1,611	0	0	1,611	1,612
C. 2014	148	0	0	148	148
D. 2015	0	0	0	0	0
E. 2016	0	0	0	0	0
F. After 5 Years	0	0	0	0	0
G. Total Future Lease Payments Due	\$ 1,759	\$ 0	\$ 0	\$ 1,759	\$ 4,173
H. Less: Imputed Interest Executory Costs	263	0	0	263	720
I. Net Capital Lease Liability	\$ 1,496	\$ 0	\$ 0	\$ 1,496	\$ 3,453
<b>2. Capital Lease Liabilities Covered by Budgetary Resources</b>				\$ 1,496	\$ 3,453
<b>3. Capital Lease Liabilities Not Covered by Budgetary Resources</b>				\$ 0	\$ 0

### **Intragovernmental Other Liabilities Composition**

Intragovernmental Other Liabilities consist of unemployment compensation liability and other unfunded employment benefits.

### **Estimated Future Contract Financing Payments**

Contingent liabilities include \$475.1 million related to contracts authorizing progress payments based on cost as defined in the Federal Acquisition Regulation (FAR). In accordance with contract terms, specific rights to the contractors' work vest with the federal government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. It is DoD policy that these rights should not be misconstrued as rights of ownership. The Army General Fund is under no obligation to pay contractors for amounts greater than the amounts of progress payments authorized in contracts until delivery and government acceptance. The Army General Fund has recognized a contingent liability for the estimated unpaid costs that are considered conditional for payment pending delivery and government acceptance for the following reasons: (1) The contractors will probably complete their efforts and deliver satisfactory products, and (2) the amount of contractor costs incurred but not yet paid are estimable.

Total contingent liabilities for progress payments based on cost represent the difference between the estimated costs incurred to date by contractors and amounts authorized to be paid under progress payments based on cost provisions within the FAR. Estimated contractor-incurred costs are calculated by dividing the cumulative unliquidated progress payments based on cost by the contract-authorized progress payment rate. The balance of unliquidated progress payments based on cost is deducted from the estimated total contractor-incurred costs to determine the contingency amount

## **NOTE 16. COMMITMENTS AND CONTINGENCIES**

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### **Information Related to Commitments and Contingencies**

The Army General Fund (GF) is a party in various administrative proceedings and legal actions related to claims for environmental damage, equal opportunity matters, and contractual bid protests.

The Army GF has accrued contingent liabilities for legal actions when the Office of General Counsel (OGC) considers an adverse decision is probable and the amount of loss is measurable. In the event of an adverse judgment against the federal government, some of the liabilities may be payable from the U.S. Treasury Judgment Fund. The Army GF reports contingent liabilities in Note 15, *Other Liabilities*.

### **Nature of Contingency**

The Management Schedule of Information derived from the FY 2012 Army Legal Representation Letter outlines claims against the Army GF totaling about \$12.0 trillion for which the Army OGC is unable to express an opinion. The majority of this amount is due to claims for the Fort Detrick, Maryland, contamination (\$10.0 trillion) and for the Hurricane Katrina levee breach (\$2.0 trillion). The historical payout percentage for these cases is less than 1 percent. To determine the historical payout, the Army OGC divides the total amount reported as a payout in the fiscal year by the total amount claimed in the Army Legal Representation Letter.

The Army GF has other contingent liabilities for which the possibility of loss is considered reasonable. These liabilities are not accrued in the Army GF's financial statements. As of September 30, 2012, the Army GF had \$576.7 million in claims considered reasonably possible. These contingent liabilities and estimates are presented in the following table. Estimates for litigations, claims, and assessments are required to be fully supported.

Estimates in the Management Schedule of Information will not always agree with amounts reported by the OGC subordinate commands, displayed below, because the Management Schedule of Information amounts are subject to a materiality threshold – currently \$32 million.



(Amounts in thousands)

Type of Contingent Liabilities	Estimate
Army Environmental Law Division	\$151,860
Army Contract Appeals	23,786
U.S. Army Claims Service	15,000
Litigation Division	386,014
<b>Total</b>	<b>\$576,660</b>

**Other Information Pertaining to Commitments**

The Army GF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of budgetary resources. Currently, the Army GF has limited automated system processes by which it captures or assesses these potential contingent liabilities; therefore, the amounts reported may not fairly present the Army GF's commitments and contingencies.

## NOTE 17. MILITARY RETIREMENT AND OTHER FEDERAL EMPLOYMENT BENEFITS

As of September 30

(Amounts in thousands)

	2012			2011	
	Liabilities	(Less: Assets Available to Pay Benefits)	Unfunded Liabilities	Unfunded Liabilities	
<b>1. Pension and Health Actuarial Benefits</b>					
A. Military Retirement Pensions	\$ 0	\$ 0	\$ 0	\$ 0	\$0
B. Military Pre Medicare-Eligible Retiree Health Benefits	0	0	0	0	0
C. Military Medicare-Eligible Retiree Health Benefits	0	0	0	0	0
D. Total Pension and Health Benefits	\$ 0	\$ 0	\$ 0	\$ 0	0
<b>2. Other Actuarial Benefits</b>					
A. FECA	\$ 1,406,105	\$ 0	\$ 1,406,105	\$ 1,356,264	
B. Voluntary Separation Incentive Programs	0	0	0	0	
C. DoD Education Benefits Fund	0	0	0	0	
D. Other	0	0	0	0	
E. Total Other Actuarial Benefits	\$ 1,406,105	\$ 0	\$ 1,406,105	\$ 1,356,264	
<b>3. Total Military Retirement and Other Federal Employment Benefits:</b>	<b>\$ 1,406,105</b>	<b>\$ 0</b>	<b>\$ 1,406,105</b>	<b>\$ 1,356,264</b>	

**Information Related to Military Retirement and Other Federal Employment Benefits****Federal Employees' Compensation Act**

The Army's actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to the Army at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred-but-not-reported claims. The actuarial liability for the Federal Employees' Compensation Act (FECA) increased \$49.8 million between FY 2011 and FY 2012.

**Actuarial Cost Method**

The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments.

**Market Value of Market-Based Securities**

As of September 30, 2012, the market value of the nonmarketable, market-based securities held by the Army General Fund (GF) was \$2.2 million. Refer to Note 4, *Investments and Related Interest*, for additional information.

## Assumptions

The projected annual benefit payments are discounted to the present value using the Office of Management and Budget's economic assumptions for 10-year U.S. Treasury notes and bonds. Cost-of-living adjustments (COLA) and consumer price index medical (CPIM) factors provided by the Department of Labor are also applied to the calculation of projected future benefits. The estimated actuarial liability is updated only at the end of each fiscal year.

Interest rate assumptions utilized for discounting were as follows:

### Discount Rates

2.293% in Year 1;

3.138% in Year 2, and thereafter

To provide more specifically for the effects of the inflation on the liability for future workers' compensation benefits, COLAs and CPIMs were applied to the calculation of projected future benefits. The actual rates for these factors for the charge-back year (CBY) 2012 were used to adjust the historical payments associated with the methodology to current year constant dollars.

The compensation COLAs and CPIMs used in the projections for various CBYs were as follows:

CBY	COLA	CPIM
2012	N/A	N/A
2013	2.83%	3.65%
2014	2.03%	3.66%
2015	1.93%	3.72%
2016	2.00%	3.73%
2017+	2.03%	3.80%

The resulting projections from the model were analyzed to ensure that the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model in comparison to economic assumptions; (2) a comparison, by agency, of the percentage change in the liability amount to the percentage change in the actual incremental payments; (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2012 to the average pattern observed during the most current three charge-back years; and (4) a comparison of the estimated liability per case in the 2012 projection to the average pattern for the projections of the most recent three years.

## Other Disclosures

Actuarial liabilities are computed for employee compensation benefits as mandated by FECA. The Office of Personnel Management provides updated Army actuarial liabilities during the 4th quarter of each fiscal year. The Army GF computes its portion of the total Army actuarial liability based on the percentage of its FECA expense to the total Army FECA expense.

## NOTE 18. GENERAL DISCLOSURES RELATED TO THE STATEMENT OF NET COST

### Intragovernmental Costs and Exchange Revenue

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
<b>Military Retirement Benefits</b>		
1. Gross Cost		
A. Intragovernmental Cost	\$ 0	\$ 0
B. Nonfederal Cost	0	0
C. Total Cost	\$ 0	\$ 0
2. Earned Revenue		
A. Intragovernmental Revenue	\$ 0	\$ 0
B. Nonfederal Revenue	0	0
C. Total Revenue	\$ 0	\$ 0
3. Losses/(Gains) from Actuarial Assumption		
Changes for Military Retirement Benefits	\$ 0	\$ 0
<b>Total Net Cost</b>	<b>\$ 0</b>	<b>\$ 0</b>

### Civil Works

1. Gross Cost		
A. Intragovernmental Cost	\$ 0	\$ 0
B. Nonfederal Cost	0	0
C. Total Cost	\$ 0	\$ 0
2. Earned Revenue		
A. Intragovernmental Revenue	\$ 0	\$ 0
B. Nonfederal Revenue	0	0
C. Total Revenue	\$ 0	\$ 0
3. Losses/(Gains) from Actuarial Assumption		
Changes for Military Retirement Benefits	\$ 0	\$ 0
<b>Total Net Cost</b>	<b>\$ 0</b>	<b>\$ 0</b>

### Military Personnel

1. Gross Cost		
A. Intragovernmental Cost	\$ 19,431,947	\$ 19,521,006
B. Nonfederal Cost	48,128,299	50,770,273
C. Total Cost	\$ 67,560,246	\$ 70,291,279
2. Earned Revenue		
A. Intragovernmental Revenue	\$ (323,754)	\$ (322,188)
B. Nonfederal Revenue	(349)	117
C. Total Revenue	\$ (324,103)	\$ (322,071)
3. Losses/(Gains) from Actuarial Assumption		
Changes for Military Retirement Benefits	\$ 0	\$ 0
<b>Total Net Cost</b>	<b>\$ 67,236,143</b>	<b>\$ 69,969,208</b>

**Intragovernmental Costs and Exchange Revenue**

As of September 30	2012		2011	
(Amounts in thousands)				
Operations, Readiness & Support				
1. Gross Cost				
A. Intragovernmental Cost	\$	29,444,338	\$	29,017,694
B. Nonfederal Cost		49,257,421		65,055,787
C. Total Cost	\$	78,701,759	\$	94,073,481
2. Earned Revenue				
A. Intragovernmental Revenue	\$		\$	3,498,400
B. Nonfederal Revenue		5,559,902		(1,201,874)
C. Total Revenue	\$	(579,196)	\$	2,296,526
3. Losses/(Gains) from Actuarial Assumption		4,980,706		
Changes for Military Retirement Benefits	\$	0	\$	0
Total Net Cost	\$	83,682,465	\$	96,370,007

**Procurement**

1. Gross Cost				
A. Intragovernmental Cost	\$	8,162,541	\$	6,755,174
B. Nonfederal Cost		23,054,079		30,607,867
C. Total Cost	\$	31,216,620	\$	37,363,041
2. Earned Revenue				
A. Intragovernmental Revenue	\$	(1,953,087)	\$	(2,008,116)
B. Nonfederal Revenue		(61,141)		18,418
C. Total Revenue	\$	(2,014,228)	\$	(1,989,698)
3. Losses/(Gains) from Actuarial Assumption				
Changes for Military Retirement Benefits	\$	0	\$	0
<b>Total Net Cost</b>	\$	29,202,392	\$	35,373,343

**Research, Development, Test & Evaluation**

1. Gross Cost				
A. Intragovernmental Cost	\$	3,013,426	\$	2,693,848
B. Nonfederal Cost		10,980,143		11,902,958
C. Total Cost	\$	13,993,569	\$	14,596,806
2. Earned Revenue				
A. Intragovernmental Revenue	\$	(4,464,361)	\$	(4,586,334)
B. Nonfederal Revenue		(107,171)		(173,483)
C. Total Revenue	\$	(4,571,532)	\$	(4,759,817)
3. Losses/(Gains) from Actuarial Assumption				
Changes for Military Retirement Benefits	\$	0	\$	0
<b>Total Net Cost</b>	\$	9,422,037	\$	9,836,989

**Intragovernmental Costs and Exchange Revenue**

As of September 30	2012		2011	
(Amounts in thousands)				
Family Housing & Military Construction				
1. Gross Cost				
A. Intragovernmental Cost	\$	1,668,213	\$	1,486,514
B. Nonfederal Cost		23,898,567		9,645,378
C. Total Cost	\$	25,566,780	\$	11,131,892
2. Earned Revenue				
A. Intragovernmental Revenue	\$	(7,651,061)	\$	(6,533,797)
B. Nonfederal Revenue		(295,541)		(193,700)
C. Total Revenue	\$	(7,946,602)	\$	(6,727,497)
3. Losses/(Gains) from Actuarial Assumption				
Changes for Military Retirement Benefits	\$	0	\$	0
Total Net Cost	\$	17,620,178	\$	4,404,395

**Consolidated**

1. Gross Cost				
A. Intragovernmental Cost	\$	61,720,465	\$	59,474,236
B. Nonfederal Cost		155,318,509		167,982,263
C. Total Cost	\$	217,038,974	\$	227,456,499
2. Earned Revenue				
A. Intragovernmental Revenue	\$	(8,832,361)	\$	(9,952,035)
B. Nonfederal Revenue		(1,043,398)		(1,550,522)
C. Total Revenue	\$	(9,875,759)	\$	(11,502,557)
3. Losses/(Gains) from Actuarial Assumption				
Changes for Military Retirement Benefits	\$	0	\$	0
4. Costs Not Assigned to Programs	\$	0	\$	0
5. (Less: Earned Revenues Not Attributed to Programs)	\$	0	\$	0
<b>Total Net Cost</b>	\$	207,163,215	\$	215,953,942

**Information Related to the Statement of Net Cost****Definitions**

Intragovernmental costs and revenue represent transactions made between two reporting entities within the federal government.

Public costs and revenue are exchange transactions made between the reporting entity and a nonfederal entity.

**Other Information Regarding Costs**

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the federal government that is supported by appropriations or other means. The intent of the SNC is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The DoD's current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The DoD is in the process of reviewing available data and developing a cost reporting methodology as required by the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, as amended by SFFAS No. 30, *Inter-entity Cost Implementation*.

The amounts presented in the Consolidated SNC are based on funding, obligation, accrual, and disbursing transactions, which are not always recorded using accrual accounting. The Army General Fund (GF) systems do not always record the transactions on an accrual basis as is required by the generally accepted accounting principles. The information presented also includes data from nonfinancial feeder systems to ensure that all cost and financing sources are captured for the Army GF.



**Additional Disclosures**

The Army GF systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side expenses are adjusted to agree with internal seller-side revenues. Expenses are generally adjusted by reclassifying amounts between federal and nonfederal expenses. Intradepartmental revenues and expenses are then eliminated.

The Army GF accounting systems do not capture information relative to heritage assets separately and distinctly from normal operations. The Army GF is not able to separately identify the costs of acquiring, constructing, improving, reconstructing, or renovating heritage assets. The Army Financial Improvement Plan outlines tasks to separately identify and report costs associated with heritage assets by 1st Quarter, FY 2013.

The abnormal revenue balance impacting the Operations, Readiness & Support Program is attributable to the current business practice which includes elimination reporting in this program group.

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## **NOTE 19. DISCLOSURES RELATED TO THE STATEMENT OF CHANGES IN NET POSITION**

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**Information Related to the Statement of Changes in Net Position****Other Financing Sources, Other**

Other Financing Sources, Other primarily consist of gains and losses that resulted from adjustments necessary to balance the Army General Fund's feeder systems with DoD's financial reporting system and to correct inherent limitations of the current financial systems

**Appropriations Received**

The Appropriations Received line item on the Statement of Changes in Net Position (SCNP) does not agree with the Appropriation line item on the Statement of Budgetary Resources (SBR). The \$2.8 billion difference is due to additional resources included in the Appropriation line item on the SBR. Refer to Note 20, *Disclosures Related to the SBR*, for further information.

**Eliminations**

In the SCNP, all offsetting balances (i.e., transfers-in and transfers-out, revenues, and expenses) for intraentity activity between Earmarked Funds and All Other Funds are reported on the same lines. The Eliminations column contains all appropriate elimination entries, which net to zero within each respective line, except for intraentity imputed financing costs.

**Earmarked Cumulative Results of Operations**

The ending balance for the Earmarked Cumulative Results of Operations on the SCNP does not agree with the Earmarked Cumulative Results reported on the Balance Sheet because the cumulative results on the Balance Sheet are presented net of eliminations.

**Change in Reporting Earmarked Funds**

On June 1, 2012, the Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards (SFFAS) 43, *Funds from Dedicated Collections*, which amended SFFAS 27, *Identifying and Reporting Earmarked Funds*. The SFFAS 43, which is effective for periods after September 30, 2012, changes the term "earmarked funds" to "funds from dedicated collections" and clarifies the criteria for their classification. Effective FY 2013, the Defense Departmental Reporting System will report all funds identified as "dedicated collections" only in the notes to the statements. Separate columns will no longer be required in the SCNP, but this statement will contain a reference to the appropriate footnotes for further information on dedicated collections.

## NOTE 20. DISCLOSURES RELATED TO THE STATEMENT OF BUDGETARY RESOURCES

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 131,871,962	\$ 139,093,091
2. Available Borrowing and Contract Authority at the End of the Period	\$ 0	\$ 0

### Information Related to the Statement of Budgetary Resources

#### Undelivered Orders

Undelivered Orders presented in the Statement of Budgetary Resources (SBR) include Undelivered Orders-Unpaid for both direct and reimbursable funds

#### Reporting of Appropriations Received

The Appropriations line on the SBR does not agree with the Appropriations Received line on the Statement of Changes in Net Position because of differences between proprietary and budgetary accounting concepts and reporting requirements. These differences, totaling \$2.8 billion, consist of the receipts for special and trust funds.

#### Presentation of Statement of Budgetary Resources

The SBR includes intraentity transactions because the statements are presented as combined.

#### Breakdown of Apportionment Categories

The amount of direct and reimbursable obligations incurred against amounts apportioned under Category A (apportioned by fiscal quarter), Category B (apportioned by project or activity), and Exempt from Apportionment is as follows:

*(Amounts in billions)*

Budgetary	Direct	Reimbursable
Category A	\$181.5	\$3.9
Category B	\$55.1	\$27.2
Exempt from Apportionment	*	**
<b>Total</b>	<b>\$236.7</b>	<b>\$31.1</b>

*(Amount in thousands)*

Non-Budgetary	Direct	Reimbursable
Category A	-	-

\* The Exempt from Apportionment amount is \$4.6 million.

\*\* The Exempt from Apportionment amount is \$0.1 million.

The above disclosure agrees (1) with the aggregate of the related information as reported on the Standard Form (SF) 133, *Report on Budget Execution* and (2) with Obligations Incurred as reported on the SBR.

The use of unobligated balances of the expired funding is restricted by time limit, purpose, and obligation limitations.

## Terms of Borrowing Authority

Borrowing authority is used for guaranteed loan defaults relating to the Armament Retooling and Manufacturing Support (ARMS) Initiative. This initiative is designed to encourage commercial use of inactive Army General Fund (GF) ammunition plants through many incentives for businesses willing to locate to a government ammunition production facility. The Army GF, by means of ARMS Initiative legislation, established a loan guarantee program to facilitate commercial firms' use of specified ammunition manufacturing facilities. The Army GF and Department of Agriculture Rural Business-Cooperative Service (RBS) established a memorandum of understanding for the RBS to administer the ARMS Initiative Loan Guarantee Program.

Borrowings are repaid on SF 1151, *Nonexpenditure Transfer Authorization*, as maturity dates become due. For liquidating accounts, maturity dates are one working day prior to the anniversary date of the note. For financing accounts, maturity dates are based on the period of time used in the subsidy calculation, not the contractual term of the agency's loans to borrowers.

There was no borrowing authority available as of September 30, 2012.

## NOTE 21. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

As of September 30	2012		2011	
(Amounts in thousands)				
<b>Resources Used to Finance Activities:</b>				
Budgetary Resources Obligated:				
1. Obligations incurred	\$	267,822,441	\$	283,449,288
2. Less: Spending authority from offsetting collections and recoveries (-)		(62,187,722)		(53,503,245)
3. Obligations net of offsetting collections and recoveries	\$	205,634,719	\$	229,946,043
4. Less: Offsetting receipts (-)		828,530		(856,292)
5. Net obligations	\$	206,463,249	\$	229,089,751
Other Resources:				
6. Donations and forfeitures of property	\$	35,024	\$	237
7. Transfers in/out without reimbursement (+/-)		4,357,168		1,800,665
8. Imputed financing from costs absorbed by others		1,043,601		1,283,044
9. Other (+/-)		(22,178,368)		(10,434,410)
10. Net other resources used to finance activities	\$	(16,742,575)	\$	(7,350,464)
11. Total resources used to finance activities	\$	189,720,674	\$	221,739,287
<b>Resources Used to Finance Items Not Part of the Net Cost of Operations:</b>				
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:				
12a. Undelivered Orders (-)	\$	628,452	\$	(2,395,513)
12b. Unfilled Customer Orders		1,104,954		1,717,357
13. Resources that fund expenses recognized in prior periods (-)		(2,052,694)		(2,704,006)
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations		(827,667)		856,567
15. Resources that finance the acquisition of assets (-)		(14,240,034)		(24,555,719)
16. Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations:				
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)		0		0
16b. Other (+/-)		17,786,177		8,633,510
17. Total resources used to finance items not part of the Net Cost of Operations	\$	2,399,188	\$	(18,447,804)
18. Total resources used to finance the Net Cost of Operations	\$	192,119,862	\$	203,291,483

As of September 30	2012		2011	
(Amounts in thousands)				
<b>Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period:</b>				
<b>Components Requiring or Generating Resources in Future Periods:</b>				
19. Increase in annual leave liability	\$	42,899	\$	182,781
20. Increase in environmental and disposal liability		0		0
21. Upward/downward reestimates of credit subsidy expense (+/-)		0		0
22. Increase in exchange revenue receivable from the public (-)		66,223		(33,360)
23. Other (+/-)		872,982		673,693
24. Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	\$	982,104	\$	823,114
<b>Components Not Requiring or Generating Resources:</b>				
25. Depreciation and amortization	\$	12,109,975	\$	16,375,441
26. Revaluation of assets or liabilities (+/-)		0		(34,774)
27. Other (+/-)				
27a. Trust Fund exchange revenue		0		0
27b. Cost of goods sold		0		0
27c. Operating material and supplies used		(513)		0
27d. Other		1,951,787		(4,501,324)
28. Total Components of Net Cost of Operations That Will Not Require or Generate Resources	\$	14,061,249	\$	11,839,343
29. Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period	\$	15,043,353	\$	12,662,457
<b>30. Net Cost of Operations</b>	\$	207,163,215	\$	215,953,940

### Information Related to the Reconciliation of Net Cost of Operations to Budget

#### Required Disclosures

Due to the limitations of the Army General Fund (GF) financial systems, budgetary data do not agree with proprietary expenses and capitalized assets. The difference between budgetary and proprietary data is a previously identified deficiency.

The amount of the adjustment to the note schedule to bring it into balance with the Statement of Net Cost totaled \$9.6 billion and was reported in the category of Other Components Not Requiring or Generating Resources.

The Reconciliation of Net Cost of Operations to Budget is intended to explain and define the relationship between net obligations from budgetary accounting and net cost of operations from proprietary accounting. The following Reconciliation of Net Cost of Operations to Budget lines is presented as combined instead of consolidated due to intraagency budgetary transactions not being eliminated:

- Obligations Incurred
- Less: Spending authority from offsetting collections and recoveries
- Obligations net of offsetting collections and recoveries
- Less: Offsetting Receipts
- Net Obligations
- Undelivered Orders
- Unfilled Customer Orders

Budgetary Resources Obligated, Other include (1) other gains and losses and (2) gains and losses on disposition of assets. These latter gains and losses resulted from adjustments necessary to balance the Army GF's feeder systems with DoD's financial reporting system and to correct inherent limitations of the current financial systems.

Other Resources or Adjustments to Net Obligated Resources That Do not Affect Net Cost of Operations, Other include financing sources transferred in and out without reimbursement, other gains and losses, and gains and losses on disposition of assets.

Components Requiring or Generating Resources in Future Period, Other represent increases in future-funded expenses for conventional disposal costs and contingent liabilities for contract appeals and tort claims.

Components not Requiring or Generating Resources, Other are comprised of other expenses not requiring budgetary resources for the Iraqi Relief and Reconstruction Fund—a transfer fund in which the Army GF executes the funding on behalf of the Executive Office of the President. The U.S. Treasury requires that the execution for this type of transfer is presented on the Army GF financial statements. This line also includes the current year change in Construction-in-Progress balances.

## NOTE 22.DISCLOSURES RELATED TO INCIDENTAL CUSTODIAL COLLECTIONS

The Army General Fund does not collect incidental custodial revenues.

## NOTE 23.EARMARKED FUNDS

BALANCE SHEET As of September 30 (Amounts in thousands)	2012				
	Military Retirement Fund	Medicare-Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
<b>ASSETS</b>					
Fund Balance with Treasury	\$ 0	\$ 0	\$ 35,147	\$ 0	\$ 35,147
Investments	0	0	2,181	0	2,181
Accounts and Interest Receivable	0	0	0	0	0
Other Assets	0	0	114	0	114
<b>Total Assets</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 37,442</b>	<b>\$ 0</b>	<b>\$ 37,442</b>
<b>LIABILITIES and NET POSITION</b>					
Military Retirement Benefits and Other Federal Employment Benefits	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Other Liabilities	0	0	1,230	0	1,230
<b>Total Liabilities</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 1,230</b>	<b>\$ 0</b>	<b>\$ 1,230</b>
Unexpended Appropriations	0	0	0	0	0
Cumulative Results of Operations	0	0	36,212	0	36,212
<b>Total Liabilities and Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 37,442</b>	<b>\$ 0</b>	<b>\$ 37,442</b>
<b>STATEMENT OF NET COST</b>					
<b>For the period ended September 30</b>					
Program Costs	\$ 0	\$ 0	\$ 26,197	\$ 0	\$ 26,197
Less: Earned Revenue	0	0	(44)	0	(44)
<b>Net Program Costs</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 26,153</b>	<b>\$ 0</b>	<b>\$ 26,153</b>
Less: Earned Revenue Not Attributable to Programs	0	0	0	0	0
<b>Net Cost of Operations</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 26,153</b>	<b>\$ 0</b>	<b>\$ 26,153</b>
<b>STATEMENT OF CHANGES IN NET POSITION</b>					
<b>For the period ended September 30</b>					
Net Position Beginning of the Period	\$ 0	\$ 0	\$ 49,586	\$ 0	\$ 49,586
Net Cost of Operations	\$ 0	\$ 0	\$ 26,153	\$ 0	\$ 26,153
Budgetary Financing Sources	0	0	4,001	0	4,001
Other Financing Sources	0	0	8,778	0	8,778
<b>Change in Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ (13,374)</b>	<b>\$ 0</b>	<b>\$ (13,374)</b>
<b>Net Position End of Period</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 36,212</b>	<b>\$ 0</b>	<b>\$ 36,212</b>



**BALANCE SHEET**  
**As of September 30**  
*(Amounts in thousands)*
**ASSETS**

	2011				
	Military Retirement Fund	Medicare-Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
Fund Balance with Treasury	\$ 0	\$ 0	\$ 47,140	\$ 0	\$ 47,140
Investments	0	0	3,205	0	3,205
Accounts and Interest Receivable	0	0	0	0	0
Other Assets	0	0	0	0	0
<b>Total Assets</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 50,345</b>	<b>\$ 0</b>	<b>\$ 50,345</b>

**LIABILITIES and NET POSITION**

Military Retirement Benefits and Other Federal Employment Benefits	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Other Liabilities	0	0	759	0	759
<b>Total Liabilities</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 759</b>	<b>\$ 0</b>	<b>\$ 759</b>
Unexpended Appropriations	0	0	0	0	0
Cumulative Results of Operations	0	0	49,586	0	49,586
<b>Total Liabilities and Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 50,345</b>	<b>\$ 0</b>	<b>\$ 50,345</b>

**STATEMENT OF NET COST****For the period ended September 30**

Program Costs	\$ 0	\$ 0	\$ 15,559	\$ 0	\$ 15,559
Less: Earned Revenue	0	0	(154)	0	(154)
<b>Net Program Costs</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 15,405</b>	<b>\$ 0</b>	<b>\$ 15,405</b>
Less: Earned Revenue Not Attributable to Programs	0	0	0	0	0
<b>Net Cost of Operations</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 15,405</b>	<b>\$ 0</b>	<b>\$ 15,405</b>

**STATEMENT OF CHANGES IN NET POSITION****For the period ended September 30**

Net Position Beginning of the Period	\$ 0	\$ 0	\$ 58,686	\$ 0	\$ 58,686
Net Cost of Operations	0	0	15,405	0	15,405
Budgetary Financing Sources	0	0	9,137	0	9,137
Other Financing Sources	0	0	(2,832)	0	(2,832)
<b>Change in Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ (9,100)</b>	<b>\$ 0</b>	<b>\$ (9,100)</b>
<b>Net Position End of Period</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 49,586</b>	<b>\$ 0</b>	<b>\$ 49,586</b>

**Information Related to Earmarked Funds**

Earmarked Funds represent funds received from outside sources for specific purposes. The Army General Fund (GF) receives earmarked funds for the following appropriations:

Sale of Hunting and Fishing Permits. Fees are received from individuals for the issuance of special hunting and fishing permits. The funds for this account are used for wildlife, fish, and game conservation and rehabilitation on military reservations. Title 10, United States Code (USC) 670b gives the authority to collect and distribute funds for the intended purposes.

Restoration of Rocky Mountain Arsenal. Funds are received from private industry for the cleanup of contaminated areas of Rocky Mountain Arsenal. Public Law (PL) 99 661, Section 1367, provides the authority for this explicit use.

Royalties for Use of DoD-Military Insignia and Trademarks. Funds are received from the sale of commemorative memorabilia, trademarks, and licensing activities. The funds are used to replenish inventory stock for such items and other related commemorative program expenses. The authority to create expenditures originates from PL 102 484, Section 378.

Forest and Wildlife Conservation, Military Reservations. Funds are received from the sales of forest products harvested from forests on military installations and distributed to the respective states involved in the sales. Each state is entitled to 40 percent of the sales of products from its forest after reimbursement of DoD appropriations for the costs of production. Title 10, USC 2665 provides authority for this fund and for payments to the states.

National Science Center. Funds received from the collection of fees are used for the operation and maintenance of the National Science Center as authorized under PL 99-145, Defense Authorization Act, 1986, Section 1459.

Bequest of Major General Fred C. Ainsworth to Walter Reed Army Medical Center. Funds received from interest on investments are used for purchasing supplies and equipment for the library at the Walter Reed Army Medical Center. The Army cannot currently identify the statutory citation that provides authority for the use of this fund. The appropriation for this earmarked fund is 21X8063.

Department of the Army General Gift Fund. Funds are received from private parties and estates and used for various purposes. Title 10, USC 2601 establishes the authority governing the use of this fund.

On June 1, 2012, the Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards (SFFAS) 43, *Funds from Dedicated Collections*, which amended SFFAS 27, *Identifying and Reporting Earmarked Funds*. The SFFAS 43, which is effective for periods after September 30, 2012, changes the term “earmarked funds” to “funds from dedicated collections.” In 1st Quarter, FY 2013, the Army GF will report its dedicated collections in accordance with SFFAS 43 requirements.

## NOTE 24. FIDUCIARY ACTIVITIES

As of September 30	2012		2011	
(Amounts in thousands)				
1. Fiduciary Net Assets, beginning of year	\$	129,380	\$	119,885
2. Fiduciary Revenues	\$	0	\$	0
3. Contributions		126,011		180,725
4. Investment Earnings		9,624		11,677
5. Gain (Loss) on Disposition of Investments, Net		0		0
6. Administrative and Other Expenses		0		0
7. Distributions to and on behalf of beneficiaries		(169,594)		(182,908)
8. Increase/Decrease in Fiduciary Net Assets	\$	(33,959)	\$	9,494
9. Fiduciary Net Assets, end of period	\$	95,421	\$	129,379

As of September 30	2012		2011	
(Amounts in thousands)				
Fiduciary Assets				
1. Cash and Cash Equivalents	\$	95,421	\$	129,380
2. Investments		0		0
3. Other Assets		0		0
Fiduciary Liabilities				
4. Less: Liabilities		0		0
5. Total Fiduciary Net Assets	\$	95,421	\$	129,380

### Information Related to Fiduciary Activities

Fiduciary activities are those federal government activities that relate to the collection or receipt of cash or other assets in which nonfederal individuals or entities have an ownership interest that the federal government must uphold. Fiduciary activities also include managing, protecting, accounting for, investing, and disposing of such cash or other assets. The DoD has a fiduciary duty to the Savings Deposit Program in which the Army General Fund (GF) participates. Public Law 89-538 authorizes DoD, through the Savings Deposit Program, to collect a voluntary allotment from the current pay of members of the armed forces deployed outside the United States or its possessions in designated areas. The Army GF collects the savings and allotments of soldiers, and the collections and accrued earned interest are transferred to the Navy General Fund, the program's executive agent. These fiduciary assets are not assets of the Army GF and are not recognized on its Balance Sheet.

## NOTE 25. OTHER DISCLOSURES

**As of September 30**

*(Amounts in thousands)*

### 1. ENTITY AS LESSEE-Operating Leases

Future Payments Due

Fiscal Year

	2012			
	Land and Buildings	Equipment	Other	Total
2013	\$ 67	\$ 0	\$ 0	\$ 67
2014	67	0	0	67
2015	67	0	0	67
2016	67	0	0	67
2017	67	0	0	67
After 5 Years	15,084	0	0	15,084
<b>Total Future Lease Payments Due</b>	<b>\$ 15,419</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 15,419</b>

## NOTE 26. RESTATEMENTS

Not applicable.



## FY 2012 REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION

The following summarizes nonfederal physical property. Investments in non-federal physical property refers to those expenses incurred by the Army for the purchase, construction, or major renovation of physical property owned by state and local governments, including major additions, alterations, and replacements; the purchase of major equipment; and the purchase of improvement to other physical assets. A schedule of estimated investments value of state-owned properties that are used by the federal government is shown below.

### Nonfederal Physical Property: Yearly Investments in State and Local Governments for Fiscal Years 2008 through 2012

(Amounts in millions)

(a)	(b)	(c)	(d)	(e)	(f)
Categories	FY 2012	FY 2011	FY 2010	FY 2009	FY 2008
<b>Transferred Assets:</b>					
1. National Defense Mission Related	\$32.4	\$31.5	\$22.2	\$26.7	\$34.2
<b>Funded Assets:</b>					
2. National Defense Mission Related	0	0	0	0	0
<b>Totals</b>	<b>\$32.4</b>	<b>\$31.5</b>	<b>\$22.2</b>	<b>\$26.7</b>	<b>\$34.2</b>

The Army General Fund (GF) incurs investments in nonfederal physical property for the purchase, construction, or major renovation of physical property owned by state and local governments, including major additions, alterations, and replacements; the purchase of major equipment; and the purchase or improvement of other nonfederal assets. In addition, nonfederal physical property investments include federally-owned physical property transferred to state and local governments.

Investment values included in this report are based on nonfederal physical property outlays (expenditures). Outlays are used because current DoD accounting systems are unable to capture and summarize costs in accordance with federal accounting standards.

The following table summarizes basic research, applied research, and development investments and provides examples of each.

### Yearly Investments in Research and Development for Fiscal Years 2008 through 2012

(Amounts in millions)

(a)	(b)	(c)	(d)	(e)	(f)
Categories	FY 2012	FY 2011 <sup>1</sup>	FY 2010	FY 2009	FY 2008
<b>Basic Research</b>	\$356.5	\$414.4	\$405.5	\$392.7	\$345.9
<b>Applied Research</b>	1,102.4	1,161.6	728.3	1,191.1	1,147.4
<b>Development</b>					
Advanced Technology Development	1,151.0	1,187.2	941.0	1,341.8	1,336.5
Advanced Component Development and Prototypes	737.3	989.9	781.3	1,023.8	719.8
Systems Development and Demonstration	2,823.8	3,424.0	1,913.7	4,883.9	4,981.4
Research, Development, Test and Evaluation Management Support	1,320.6	1,397.4	726.3	1,387.1	1,317.1
Operational Systems Development	1,173.4	1,291.0	690.2	1,700.9	1,459.2
<b>Totals</b>	<b>\$8,665.0</b>	<b>\$9,865.5</b>	<b>\$6,186.3</b>	<b>\$11,921.3</b>	<b>\$11,307.3</b>

Note 1: The amounts reported at 4th Quarter, FY 2011 for Yearly Investments in Research and Development were incorrect due to calculation errors. The correct numbers are shown above.

### Narrative Statement

Research and development (R&D) programs are classified in the following categories: basic research, applied research, and development. The definition for each type of R&D category and subcategories is explained below.

Basic Research is the systematic study to gain knowledge or understanding of the fundamental aspects of phenomena and observable facts without specific applications, processes, or products in mind. Basic research involves the gathering of a fuller knowledge or understanding of the subject under study. Major outputs are scientific studies and research papers.

*The following are two representative program examples for each of the major categories:*

Defense Research Sciences (PE 0601102A): This program fosters fundamental scientific knowledge and contributes to the sustainment of Army scientific and technological superiority in land warfighting capability; provides new concepts and technologies for the Army's future force; and provides the means to exploit scientific breakthroughs and avoid technological surprises. It fosters innovation in Army niche areas (such as lightweight armor, energetic materials, night vision) and when the commercial incentive to invest is lacking due to limited markets, e.g., vaccines for tropical diseases. It also focuses universal single investigators on research areas of Army interest, such as high-density compact power and novel sensor phenomenologies. The in-house portion of the program capitalizes on the Army's scientific talent and specialized facilities to expeditiously transition knowledge and technology into the appropriate developmental activities. The extramural program leverages the research efforts of other government agencies, academia, and industry. This translates to a coherent, well-integrated program which is executed by four primary contributors: (1) the Army Research, Development, and Engineering Command; (2) the U.S. Army Engineer Research and Development Center; (3) the Army Medical Research and Materiel Command laboratories; and, (4) the Army Research Institute for Behavioral and Social Sciences. The basic research program is coordinated with the other services via Defense Science and Technology Reliance (Defense Basic Research Advisory Group) and other inter-service working groups. This program responds to the scientific and technological requirements of the DoD Basic Research Plan by enabling technologies that can significantly improve joint war-fighting capabilities. The projects in this program involve basic research efforts directed toward providing fundamental knowledge that will contribute to the solution of military problems related to long-term national security needs.

University and Industry Research Centers (PE 0601104A): A significant portion of the work performed within this program directly supports future force requirements by providing research that supports enabling technologies for future force capabilities. Broadly, the work in this project falls into three categories: collaborative technology alliances (CTAs), university centers of excellence (COEs), and paradigm-shifting centers, university-affiliated research centers (UARCs). The Army has formed CTAs to leverage large investments by the commercial sector in basic research areas that are of great interest to the Army. The CTAs involve partnerships among industry, academia, and the Army Research Laboratory (ARL) to incorporate the practicality of industry; the expansion of the boundaries of knowledge from universities; and the ability of Army scientists to shape, mature and transition technology. The CTAs have been competitively established in the areas of advanced sensors, advanced decision architecture, communications and networks, power and energy, and robotics. This program element includes the Army's COEs, which focus on expanding the frontiers of knowledge in research areas where the Army has enduring needs, such as rotorcraft, automotive, microelectronics, materials, and information sciences. The COEs couple state-of-the-art research programs at academic institutions with broad-based graduate education programs to increase the supply of scientists and engineers in information sciences, materials science, electronics, automotive, and rotary-wing technology. Also included is eCYBERMISSION, the Army's national, web-based competition to stimulate interest in science, math, and technology among middle and high school students. This program also includes the four Army UARCs, which have been created to exploit opportunities to advance new capabilities through a sustained long-term, multi-disciplinary effort. The Institute of Advanced Technology funds basic research in electromagnetics and hypervelocity physics. The Institute for Soldier Nanotechnologies (ISN) focuses on Soldier protection by emphasizing revolutionary materials research for advanced Soldier protection and survivability. The Institute for Collaborative Biotechnologies, focusing on enabling network-centric technologies, will broaden the Army's use of biotechnology for the development of bio-inspired materials, sensors, and information processing. The Institute for Creative Technologies is a partnership with academia and the entertainment and gaming industries to leverage innovative research and concepts for training and simulation.

Applied Research is the systematic study to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met. It is the practical application of such knowledge or understanding for the purpose of meeting a recognized need. This research points toward specific military needs with a view toward developing and evaluating the feasibility and practicability of proposed solutions and determining their parameters. Major outputs are scientific studies, investigations, research papers, hardware components, software codes, and limited construction of, or part of, a weapon system to include non-system specific development efforts.

*The following are two representative program examples for this category:*

Materials Technology (PE 0602105A): This program funds research and evaluation of materials technologies for armor and armaments that will significantly enhance the survivability and lethality of future force systems and, when feasible, can be exploited to enhance the current force. This program builds on materials research transitioned from the Defense Research Sciences Materials and Mechanics



Project and applies it to specific Army platforms and the individual Soldier. This program is directed toward developing materials technology that contributes to making heavy forces lighter and more deployable and light forces more lethal and survivable. The program provides the technology base required for solving materials-related problems in individual Soldier support equipment, armor, armaments, aircraft, ground and combat vehicles, and combat support. This program also funds collaborative research efforts in nanomaterials technology among the ARL, the ISN at the Massachusetts Institute of Technology, and the ISN industry partners. The effort is focused specifically on the improvement in individual Soldier protection.

Combat Vehicle and Automotive Technology (PE 0602601A): This program researches, investigates, and applies combat vehicle and automotive component technologies that enhance survivability, mobility, sustainability, and maintainability of Army ground combat and tactical vehicles. As combat vehicle systems become smaller and lighter, and tactical vehicles are more often exposed to combat conditions, one of the greatest technological and operational challenges is providing adequate crew protection without reliance on heavy, passive armor. This challenge will be met using a layered approach, including long-range situational awareness, advanced lightweight opaque and transparent armors, active protection systems, and multi-spectral signature reduction. Another focus of the program is on designing, fabricating, and evaluating performance of integrated and add-on lightweight armor packages needed to provide lightweight combat vehicles protection against chemical energy and kinetic energy threats with less than one-fourth the weight of conventional heavy armor. Additionally, the program is organized to design, fabricate, and evaluate structural and add-on armors for tactical vehicles. This program funds the National Automotive Center (NAC). The goal of the NAC is to leverage large, commercial investments in automotive technology, research, and development by pursuing automotive-oriented technology programs that have potential benefit to military ground vehicles. The research and investigation of a variety of enabling technologies in the areas of hybrid electric propulsion, mobility, thermal management, intelligent systems, vehicle diagnostics, fuels/lubricants, and water purification is also part of the program function. Future force vehicles and new tactical vehicles are being designed with hybrid electric architectures, advanced high-power density engines, and auxiliary power units that provide power for propulsion, control systems, communications, life support systems, electromagnetic armor, Soldier battery charging, and export to other systems.

Development takes what has been discovered or learned from basic and applied research and uses it to establish technological feasibility, assessment of operability, and production capability. Development is comprised of the five stages defined below; program examples follow:

1. Advanced Technology Development is the systematic use of the knowledge or understanding gained from research directed toward proof of technological feasibility and assessment of operations and productibility rather than the development of hardware for service use. It employs demonstration activities intended to prove or test a technology or method.
2. Advanced Component Development and Prototypes (ACD&P) evaluates integrated technologies in as realistic an operating environment as possible to assess the performance or cost reduction potential of advanced technology. Programs in this phase are generally system specific. Major outputs of ACD&P are hardware and software components, or complete weapon systems ready for operational and developmental testing and field use.
3. System Development and Demonstration concludes the program or project and prepares it for production. It consists primarily of pre-production efforts, such as logistics and repair studies. Major outputs are weapons systems finalized for complete operational and developmental testing.
4. Research, Development, Test & Evaluation Management Support is support for installations and operations for general R&D use. This category includes costs associated with test ranges, military construction maintenance support for laboratories, operation and maintenance of test aircraft and ships, and studies and analyses in support of the R&D program.
5. Operational Systems Development is concerned with development projects in support of programs or upgrades still in engineering and manufacturing development, which have received approval for production, and for which production funds have been budgeted in subsequent fiscal years.

Electronic Warfare Advanced Technology (PE 0603008A): The goal of this program is to provide the Army's future force enabling technologies for a secure, mobile, wireless network that will operate reliably in diverse and complex terrain, in all environments, and, when feasible, to exploit opportunities to enhance current force capabilities. Technologies will be matured and demonstrated to address this challenge with distributed, mobile, secure, self-organizing communications networks. A key objective is to demonstrate seamlessly integrated communications technologies across all network tiers, ranging from unattended networks and sensors through maneuver elements and airborne/space assets. To accomplish the goal, this program will investigate and leverage external communication technologies and combine technology options in a series of command, control, communications, and computers intelligence,

surveillance, and reconnaissance on-the-move experiments to measure the battlefield effectiveness for the future force. This program also provides (1) protection technologies for tactical wireless networks against modern network attacks; (2) smart communication technologies to network and control unmanned systems anywhere on the battlefield, enabling timely sensor-decider-engagement linkage to defeat critical targets; (3) advanced antenna technologies for greater communications mobility, range, and throughput; and, (4) automated network management aids.

Aviation - Advanced Development (PE 0603801A): This program provides advanced development aviation support of tactical programs associated with air mobility, advanced maintenance concepts and equipment, and Aircrew Integrated Systems. This program demonstrates the feasibility and maturity of new technology and gains understanding in order to evaluate utility of this technology to expedite delivery of new capabilities for Army aviation rotary-wing assets. Additionally, the aviation ground support equipment assets enhance the functionality of current and future aircraft by (1) improving the effectiveness of maintenance and servicing operations through validating new maintenance concepts to improve man and machine interfaces; (2) improving aircraft maintenance processes; (3) reducing operation and support costs; , and, (4) inserting diagnostics technologies to replace obsolete and unsupportable equipment.

Patriot/Medium Extended Air Defense System Combined Aggregate Program (CAP) (PE 0604869A): The Medium Extended Air Defense System (MEADS) program is a tri-national, co-development program among the United States, Germany, and Italy to replace the U.S. Patriot air defense systems, Patriot and Hawk systems in Germany, and Nike Hercules systems in Italy. The North Atlantic Treaty Organization (NATO) MEADS Management Agency (NAMEADSMA) is the NATO contracting authority that manages the system acquisition, and the MEADS program, itself, on behalf of participating nations. Within the Patriot/MEADS CAP, there are two synergistic efforts: (1) an international MEADS development effort managed by NAMEADSMA; and, (2) a U.S. effort to inject U.S.-specific capability requirements into the MEADS major end items. The MEADS will provide joint and coalition forces with critical asset and defended area protection against multiple and simultaneous attacks by short- to medium-range ballistic missiles, cruise missiles, unmanned aerial vehicles and tactical air-to-surface missiles. The Missile Segment Enhancement (MSE) missile has been accepted as the baseline missile for MEADS. It is being developed for the Patriot system to meet U.S. operational requirements. The MSE will provide a more agile and lethal interceptor that increases the engagement envelope/defended area of the Patriot and the MEADS systems. The Patriot Advanced Capability-3 (PAC-3) MSE improves upon the current PAC-3 missile capability by providing a higher performance solid rocket motor, modified lethality enhancer, more responsive control surfaces, upgraded guidance software, and insensitive munitions improvements.

Army Test Ranges and Facilities (0605601A): This program funds the indirect test costs associated with rapidly-testing field systems and equipment needed in support of the War on Terror, such as individual Soldier protection equipment and countermeasures for improvised explosive devices and up-armoring the Army's wheeled vehicle fleet. This project sustains the developmental test and evaluation capability required to support Army as well as joint service or other service systems' hardware and technologies. Unclassified systems scheduled for developmental testing encompass the entire spectrum of weapons systems. Capabilities are also required to support system-of-systems and network-centric systems to include future combat system testing.

This project provides the institutional funding required to operate the developmental test activities required by DoD program executive officers; program and product managers; and research, development, and engineering centers. This project resources four DoD major range and test facility bases: White Sands Missile Range, New Mexico; Aberdeen Test Center, Maryland; Electronic Proving Ground, Arizona; and Yuma Proving Ground, Arizona, and includes management of natural environmental testing at Cold Regions Test Center, Fort Greely and Fort Wainwright, Alaska, and the Tropic Regions Test Center at various locations. This project also funds the Army's developmental test capability at Aviation Technical Test Center and Redstone Technical Test Center, both in Alabama. Test planning and safety verification at Headquarters, U.S. Army Developmental Test Command, Maryland, is also supported by this program.

Information Systems Security Program (0303140A): The Communications Security Equipment Program develops information systems security (ISS) equipment and techniques required to combat threat signal intelligence capabilities and to ensure the integrity of data networks. The Army's Research, Development, Test, and Evaluation ISS program objective is to implement National Security Agency-developed security technology in Army information systems. Communications security equipment technology ensures total signal and data security for all Army information systems to include any operational enhancement and specialized configurations.

National Defense Property, Plant, and Equipment: The Federal Accounting Standards Advisory Board revised the Statement of Federal Financial Accounting Standards No. 6 to require the capitalization and depreciation of military equipment (formerly National Defense Property, Plant and Equipment) for Fiscal Year 2003 and beyond, and encouraged early implementation.

## FISCAL YEAR 2012 REQUIRED SUPPLEMENTARY INFORMATION

### General Property, Plant, and Equipment Real Property Deferred Maintenance Amounts for Fiscal Year Ended September 30, 2012

(Amounts in millions)		CURRENT FISCAL YEAR		
Property Type	Plant Replacement Value	Required Work (deferred maintenance)	Percentage	
Category 1	\$231,826	\$32,237	14%	
Category 2	\$14,723	\$5,010	34%	
Category 3	\$7,702	\$0	0%	

### Narrative Statement

In accordance with DoD Financial Management Regulation 7000.14-R (updates through February 2012), Volume 6B, Chapter 12, Paragraph 120303. B.1., the Army's FY 2012 deferred maintenance estimates include all facilities in which DoD has ownership interest under the control of the Army. Previous deferred maintenance estimates did not include nonArmy assets.

The deferred maintenance estimates are based on the facility Q-ratings reported in the Installation Status Report (ISR) for 4th Quarter, FY 2012 or Q-ratings obtained by application of business rules described below. For FY 2012, the Q-rating values range from 0 to 100. Deferred maintenance is calculated as follows:

$$\text{Deferred Maintenance} = (100 - \text{Q-rating}) \times 0.01 \times \text{plant replacement value (PRV)}.$$

Q-ratings are determined by the ISR for the majority of facilities, and by business rule for the remaining facilities. During ISR data collection, facility occupants evaluate the condition of each facility against published standards. The inspection generates a quality improvement cost estimate for each facility based on the condition rating of each component of the facility, and the component improvement cost factor. Improvement cost factors are developed using industry standards for each facility component within each facility type. The business rule assignment of Q-ratings is as follows: 95 if the facility is no more than 5 years old; 85 if the facility is permanent or semi-permanent construction and between 5 and 15 years old; 70 if the facility is permanent or semi-permanent construction and more than 15 years old; 40 if the facility is temporary construction and more than 5 years old; 95 if the asset is a lease. Acceptable operating condition represents facilities with no deferred maintenance.

Facilities with an ownership interest of "FEE" are included in the data set.

*Property Categories are as follows:*

- Category 1: Buildings, structures, and utilities that are enduring and required to support an ongoing mission including multi-use heritage assets. (Facilities with an operational status of Active or Semi-Active are included, less those with a disposal code.)
- Category 2: Buildings, structures, and utilities that are excess to requirements or planned for replacement or disposal including multi-use heritage assets. (Facilities with an operational status of Caretaker, Disposed, Excess, Non-Functional, Outgrant, and Surplus plus Active and Semi-active with disposal codes.)
- Category 3: Buildings, structures, and utilities that are heritage assets. These have an operational status of Closed and are not maintained. (Facilities with an operational status of Closed as well as a historical status.)

**Military Equipment Deferred Maintenance for Fiscal Year Ended September 30, 2012**  
(Amounts in thousands)

MAJOR CATEGORIES	
Aircraft	\$27,116
Automotive Equipment	37,910
Combat Vehicles	26,622
Construction Equipment	0
Electronics and Communications Systems	144,503
General Purpose Equipment	20,444
Missiles	27,389
Ordnance Weapons and Munitions	10,806
Other	12,600
Ships	0
<b>Grand Total</b>	<b>\$307,390</b>

The OP-30 from the FY 2012 president's budget was used to compile the deferred depot level maintenance.

The Depot Maintenance Operations and Planning System is the automated system for capturing depot-level deferred maintenance data. The data is for subactivity group 123, all active components.

Funding provided to support the Program Objective Memorandum (POM) 12-16 for depot maintenance adequately supported the Army's most critical modernization and equipping strategies. The program ensured that Soldiers have the equipment needed to execute their assigned mission as they progress through the Army Force Generation (ARFORGEN) cycle. The bottom-line is that depot maintenance requirements continue to grow while the Army continues to get fewer resources with reduced budgets.

The funding also provided the resources necessary for land forces depot maintenance to meet the requirements of an Army transitioning from operations in theater to home station training – an expeditionary Army engaged in full spectrum operation (FSO) training and poised for future contingency response. In recent years, the Army has leveraged overseas contingency operation (OCO) dollars to offset depot maintenance through equipment reset for redeploying units. Deployed units and enduring equipment requirements currently funded by OCO will accelerate their transition into the base budget as operations in Southwest Asia continue decreasing. Redeployed units will demand greater equipment to support FSO training and future contingencies. To meet the exigencies of war, Army has generated a digitally dependent force. The digitally integrated Army of today is far different from the analog Army that went to war at the beginning of the decade. These technologies must now be sustained.

The FY 2012 base budget includes two congressional realignments: approximately \$1 billion and \$188 million base requirements to OCO. These realignments funded depot level maintenance for Army weapon systems in support of next deploying units. These programs were not an OCO requirement in FY 2013 and did not affect deferred maintenance.

Unfunded requirements totaled approximately \$1 billion. These amounts include software and cover all validated requirements that support readiness of the Army in its mission to fight and win the nation's wars. The development of the Army's requirements each year is a zero sum computation, which means that the unfunded requirement in the budget year does not roll into the next fiscal year. The FY 2012 true deferred maintenance is the difference between the total validated unfunded requirement and the critical unfunded requirement. These fleet readiness and software shortfalls include:

- Communication-electronics critical requirements, which address critical intelligence network sustainment and system maintenance, sense and warn systems that provide vital force protection.
- Post-production software support (PPSS) critical requirements that address the required software maintenance for various weapon systems.
- Test, Measurement and Diagnostic Equipment (TMDE) that addresses the calibration of TMDE to ensure weapon systems meet all of the design performance standards and ensure the health and safety of the Soldier and avoid aircraft and weapon system failures; watercraft maintenance is also addressed with this requirement.

- d. Combat systems and bridging, which provide the overhaul of the main battle tank, and tactical bridging to restore equipment reliability (National Guard).
- e. Tactical wheel vehicles that overhaul the M900 series of 5-ton trucks, the family of medium tactical vehicles, M915/6 and heavy, expanded mobility tactical-series trucks to sustain fleet readiness (National Guard and Army Reserve).

*The future POM requirements are driven by the following:*

- ⇒ Increased reliance on software and digital technology.
- ⇒ The FSO placing new demands on the industrial base.
- ⇒ Support of non-standard equipment which has been identified for sustainment as long-term force capabilities.
- ⇒ Legacy and current equipment remaining in-service for longer than anticipated.
- ⇒ New equipment and capabilities entering the sustainment phase in their lifecycles.
- ⇒ An emerging mine-resistant, ambush-protected vehicle fleet.

Over the course of the last decade, this growing presence of digital technology and its PPSS was heavily funded by OCO dollars. With limited resources, the Army has to take risks in depot maintenance and has to balance requirements with available resources. The Army has to identify critical software requirements and prioritize those that require funding to meet ARFORGEN and unit readiness requirements. In addition, the Army will rely on available OCO dollars to ensure all critical shortfalls including deferred maintenance are met.

#### **Heritage Assets and Stewardship Land Condition Information for Fiscal Year Ended September 30, 2012**

The conditions of archeological sites across the Army remain varied from poor to excellent based on a number of factors including the environmental setting and natural disasters, the type of the site, and impacts from Army activities. If an Army activity has the potential to adversely impact an archeological site eligible for the National Register of Historic Places, the Installation Cultural Resources Management Plan (ICRMP) contains provisions for how the installation might proceed to avoid, minimize, or mitigate those impacts. The ICRMPs provide installations the information and tools necessary to manage their cultural resources, including archeological sites, in compliance with federal requirements. These plans provide for site protection, site condition monitoring, and mitigation procedures for adverse impacts to sites. Overall, the conditions of sites on Army installations are fair, based on the Army's cultural resource management procedures.





**INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
4800 MARK CENTER DRIVE  
ALEXANDRIA, VIRGINIA 22350-1500**

November 8, 2012

MEMORANDUM FOR ASSISTANT SECRETARY OF THE ARMY (FINANCIAL MANAGEMENT AND COMPTROLLER)

SUBJECT: Independent Auditor's Report on the Army General Fund FY 2012 and FY 2011 Financial Statements  
(Report No. DODIG-2013-013)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Army General Fund Consolidated Balance Sheet as of September 30, 2012 and 2011, and the Consolidated Statement of Net Cost, Consolidated Statement of Changes in Net Position, Combined Statement of Budgetary Resources, and related notes for the fiscal years then ended. The financial statements are the responsibility of Army management. Management is also responsible for implementing effective internal control and for complying with laws and regulations. In addition, management is responsible for implementing and maintaining financial management systems that comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA). Our responsibility is to express an opinion on the financial statements based on our audit.

We are unable to express an opinion on the Army General Fund FY 2012 and FY 2011 Basic Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer, we are including the required report on Internal Control and Compliance with Laws and Regulations. The report is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of our work.

### **Disclaimer of Opinion on the Financial Statements**

The Deputy Assistant Secretary of the Army (Financial Operations) represented to us that the Army General Fund FY 2012 and FY 2011 Annual Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (U.S. GAAP) and that Army financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2012. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the management representations made to us. Accordingly, we did not perform all the auditing procedures required by generally accepted government auditing standards and Office of Management and Budget (OMB) Bulletin 07-04, "Audit Requirements for Federal Financial Statements," September 4, 2007, as amended<sup>1</sup> to determine whether material amounts on the financial statements were presented fairly.

Prior audits have identified, and Army management has also acknowledged, the long standing material internal control weaknesses identified in the Summary of Internal Control. These material internal control weaknesses may affect the reliability of certain information contained in the annual financial statements – much of which was taken from the same data sources.<sup>2</sup> Therefore, we are unable to express, and we do not express, an opinion on the Basic Financial Statements.

<sup>1</sup> OMB Memorandum M-09-33, Technical Amendments to OMB Bulletin No. 07-04, "Audit Requirements for Federal Financial Statement," September 23, 2009.

<sup>2</sup> The annual financial statements include the Basic Financial Statements, Management Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.



## Summary of Internal Control

In planning our work, we considered Army internal control over financial reporting and compliance with applicable laws and regulations. We did this to determine our audit procedures and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations. However, previously identified significant deficiencies, all of which are material, continue to exist in the following areas.

- Financial Management Systems
- Fund Balance with Treasury
- Accounts Receivable
- Inventory and Related Property
- General Property, Plant, and Equipment
- Accounts Payable
- Environmental Liabilities
- Statement of Net Cost
- Statement of Budgetary Resources
- Intragovernmental Eliminations
- Accounting Adjustments
- Abnormal Account Balances
- Reconciliation of Net Cost of Operations to Budget
- Contingency Payment Audit Trails

A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a deficiency or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. The following significant deficiency continued to exist:

- Legal Representation Process

Internal control work we conducted as part of our prior audits would not necessarily disclose all deficiencies. Attachment 1 offers additional details on significant deficiencies, most of which we consider to be material weaknesses.

The Army reported these 14 material weaknesses in its FY 2012 Statement of Assurance.

## Compliance with Laws and Regulations

We limited our work to determining compliance with selected provisions of applicable laws and regulations related to financial reporting because management represented that instances of noncompliance identified in prior audits continued to exist. The Deputy Assistant Secretary of the Army (Financial Operations) represented to us that the Army General Fund financial management systems do not substantially comply with Federal financial management system requirements, U.S. GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether Army General Fund management complied with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit, and accordingly, we do not express such an opinion. See Attachment 1 for additional details on compliance with laws and regulations.

## Other Information in the Annual Financial Statements

The Army General Fund Management Discussion and Analysis and Required Supplementary Information are not a required part of the basic financial statements, and we did not audit and do not express an opinion on such information. However, we have applied

certain limited procedures prescribed by auditing standards that raised doubts that we were unable to resolve regarding whether material modifications should be made to the information for it to conform with U.S. GAAP. We compared the information with the Army General Fund financial statements for consistency. Based on our limited work, we found inconsistencies between the information and the financial statements and applicable sections of OMB Circular No. A-136 (Revised), "Financial Reporting Requirements," August 3, 2012, and DoD 7000.14-R, "Financial Management Regulation," volume 6B, "Form and Content of DoD Audited Financial Statements," June 2012.

## Scope and Methodology

Management is responsible for:

- preparing financial statements that conform with U.S. GAAP;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) are met;
- ensuring that the Army financial management systems substantially comply with FFMIA requirements, and;
- complying with applicable laws and regulations.

We are responsible for planning and performing the audit to obtain reasonable assurance and to provide an opinion on whether the Army General Fund financial statements are presented fairly, in all material respects, in conformity with U.S. GAAP. We are also responsible for (1) testing whether Army financial management systems substantially comply with the three FFMIA requirements, (2) testing compliance with selected provisions of laws and regulations that have direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and (3) performing limited procedures with respect to certain other information appearing in the annual financial statements.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing over financial reporting and compliance to previously identified significant deficiencies, all of which are material and continue to exist. Because of inherent limitations in internal controls, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected.

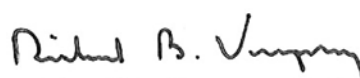
Because of the significance of the limitations on the scope of our work, we were unable to and did not perform our audit of internal control in accordance with U.S. GAAP and OMB audit guidance. We considered the limitation on the scope of our work in forming conclusions and in testing the financial statements.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

## Agency Comments and Our Evaluation

On November 5, 2012, we provided a draft of this report to the Deputy Assistant Secretary of the Army (Financial Operations). The Deputy Assistant Secretary of the Army (Financial Operations) responded in a memorandum dated November 7, 2012, which is included in its entirety at Attachment 2. The Department's response was considered in preparing the final version of this report.

This report is intended solely for the information and use of the Department's management, DoD Office of Inspector of General, OMB, Government Accountability Office, and Congress and is not intended to be used by anyone other than these specified parties.



Richard B. Vasquez, CPA  
Acting Assistant Inspector General  
Financial Management and Reporting

Attachments:  
As stated



## Report on Internal Control and Compliance with Laws and Regulations

### Internal Control

Management is responsible for implementing and maintaining effective internal control to include providing reasonable assurance that Army General Fund personnel accumulated, recorded, and reported accounting data properly; met the requirements of applicable laws and regulations; and safeguarded assets against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, the following material weaknesses and significant deficiency exist that could adversely affect the Army General Fund financial reporting.

### *Previously Identified Material Weaknesses*

Management acknowledged that it is unable to comply with applicable reporting requirements and has identified the following material weaknesses, all of which are material, that continued to exist in the following areas.

#### **Financial Management Systems**

Army accounting systems lacked a single, standard transaction-driven general ledger. The Army also needed to upgrade or replace many of its nonfinancial feeder systems so it could meet financial statement reporting requirements. The lack of a single, standard transaction-driven general ledger will continue to prevent the Army from preparing auditable financial statements.

The Army has stated that it has fully deployed the General Fund Enterprise Business System (GFEBS) with the intention of correcting existing problems and improving current processes in Army financial systems. However, until all of the Army General Fund's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by U.S. GAAP, some of the Army General Fund's financial data will be derived from budgetary transactions, data from nonfinancial feeder systems, and accruals.

Army managers also stated that GFEBS contained a chart of accounts based on the U.S. Government Standard General Ledger and created additional GFEBS subsidiary accounts that would track Army General Fund financial activities at a detailed level. However, DoD Office Inspector General Report No. DODIG-2012-066, "General Fund Enterprise Business System Did Not Provide Required Financial Information," March 26, 2012, reported that GFEBS did not contain accurate and complete FY 2010 U.S. Government Standard General Ledger and Standard Financial Information Structure information as required by FFMIA and Under Secretary of Defense (Comptroller)/Chief Financial Officer guidance. As a result, GFEBS did not provide DoD management with required financial information. The report further noted that GFEBS may not resolve the Army General Fund's long-standing Financial Management Systems material weakness. The Army does not expect to complete all corrective actions to resolve this material weakness until FY 2014.

#### **Fund Balance With Treasury**

DoD and its Components, including the Army, have had a long-standing problem reconciling transactional activity in their Fund Balance with Treasury accounts. The appropriation balances recorded in the accounting records do not agree with Treasury balances. As of September 30, 2012, the Treasury reported \$3.8 billion more in Fund Balance with Treasury than reported by the Army General Fund. The Army stated that the target date for correcting this material weakness is the third quarter of FY 2014.

#### **Accounts Receivable**

The Army has acknowledged weaknesses in its management of accounts receivable. The weaknesses are considered to be DoD-wide and apply to both public and intragovernmental receivables at the Army General Fund level. The Army's accounts receivable has weaknesses that include:

- noncompliance with policies and procedures on referrals to the Department of the Treasury's Debt Management Office and on write-offs of 2-year-old debt;
- a lack of controls to ensure that all entitlement system receivables (vendor pay, civilian pay, and interest) are recorded in the accounting systems, to include GFEBS; and
- a lack of controls to ensure that accounts receivable balances are supportable at the transaction level.

The Army stated that the target date for correcting this material weakness is the third quarter of FY 2014.

**Inventory and Related Property**

The systems do not maintain the historical cost data necessary to comply with Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." Army systems are unable to produce financial transactions using the U.S. Government Standard General Ledger. Statement No. 3 states that Operating Materials and Supplies must be expensed when the items are consumed. However, significant amounts of Operating Materials and Supplies were expensed when they were purchased instead of when they were consumed. The Army stated that the target date for correcting this material weakness is the first quarter of FY 2014.

**General Property, Plant, and Equipment**

Statement of Federal Financial Accounting Standards No. 6, "Accounting for Property, Plant, and Equipment," requires the recording of General Property, Plant, and Equipment at cost and the recognition of depreciation expense. The Army has acknowledged that they have not recorded real property and Military Equipment at acquisition or historical cost and did not include all the costs needed to bring these assets to a form and location suitable for their intended use. The Army could not support the reported cost of Military Equipment in accordance with Statement No. 6. Also, the Army's financial accountability systems for all its Military Table of Equipment unit property books do not comply with FFMIA. The Army stated that the target date for correcting this material weakness is the first quarter of FY 2014.

**Accounts Payable**

The Army is unable to account for and report Accounts Payable properly. In addition, the Army accounting systems did not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations for intra-agency sales. Therefore, the Army has acknowledged that it was unable to reconcile Intragovernmental accounts payable to the related Intragovernmental accounts receivable that generated the payable. The Army stated that the target date for correcting this material weakness is the third quarter of FY 2014.

**Environmental Liabilities**

The Army had not properly estimated and reported its environmental liabilities. For example, the processes used to report environmental liabilities for the Defense Environmental Restoration Program, Base Realignment and Closure, and the non-Defense Environmental Restoration Program on the financial statements were not adequate to establish or maintain sufficient documentation and audit trails. Although estimators qualified to perform estimates existed, the Army did not document supervisory reviews of estimates and did not have adequate quality control programs in place to ensure the reliability of data. The Army stated that the target date for correcting this material weakness is the first quarter of FY 2015.

**Statement of Net Cost**

The Army did not present financial information contained in the Statement of Net Cost by programs that align with major goals and outputs described in the DoD strategic and performance plans required by the Government Performance and Results Act of 1993 (GPRA). Because financial processes and systems did not correlate costs with performance measures, the Army reported revenues and expenses by appropriation categories. The amounts presented in the Statement of Net Cost are based on funding, obligation, and disbursing transactions, which are not always recorded using accrual accounting. Also, the Army systems did not always record the transactions on an accrual basis as required by GAAP. To capture all cost and financing sources for the Army, the information presented also includes data from the nonfinancial feeder systems. In addition, the Army General Fund budgetary and proprietary information does not correlate. The Army stated that the target date for correcting this material weakness is the third quarter of FY 2014.

**Statement of Budgetary Resources**

The Army accounting systems did not provide or capture the data needed for obligations incurred or prior-year obligations recovered in accordance with OMB Circular No. A-11, "Preparation, Submission, and Execution of the Budget Requirements." Although the Army developed an alternative methodology to calculate these items, the amount of distortion cannot be reliably determined. The information presented in the Army General Fund's Statement of Budgetary Resources does not completely agree with the information submitted in the year-end "Reports on Budget Execution and Budgetary Resources" (SFs-133).

On October 13, 2011, the Secretary of Defense directed DoD to accelerate key elements of the Financial Improvement and Audit Readiness Plan and place greater emphasis on the overall effort of achieving the Financial Improvement and Audit Readiness priorities

and auditable financial statements. Specifically, the Secretary called for the Department to achieve Statement of Budgetary Resources audit readiness by the end of FY 2014. The Army stated that the target date for correcting this material weakness is the third quarter of FY 2014.

#### **Intragovernmental Eliminations**

DoD and Army were unable to collect, exchange, and reconcile buyer and seller Intragovernmental transactions, resulting in adjustments that cannot be verified. This is primarily because the majority of the systems within DoD do not allow the capture of buyer-side information for use in reconciliations and eliminations. The DoD and Army accounting systems were unable to capture trading partner data at the transaction level to facilitate required trading partner eliminations, and DoD guidance did not require adequate support for eliminations. In addition, DoD procedures required that buyer-side transaction data be forced to agree with seller side transaction data without performing proper reconciliations. The Army stated that the target date for correcting this material weakness is the second quarter of FY 2014.

#### **Accounting Adjustments**

Because of inadequate financial management systems and processes, journal voucher adjustments and data calls were used to prepare the Army General Fund financial statements. For the FY 2012 year-end, the Defense Finance and Accounting Service did not adequately support \$110.9 billion in journal voucher adjustments used to prepare the Army General Fund financial statements. The Army stated that the target date for correcting this material weakness is the second quarter of FY 2013.

#### **Abnormal Account Balances**

The Defense Finance and Accounting Service did not detect, report, or take action to eliminate the abnormal balances included in the Army General Fund accounting records. Abnormal balances not only distort the Army General Fund financial statements, but also indicate internal control and operational deficiencies and may conceal instances of fraud. The Army stated that the target date for correcting this material weakness is the second quarter of FY 2013.

#### **Reconciliation of Net Cost of Operations to Budget**

The Statement of Federal Financial Accounting Standards No. 7, "Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting," requires a reconciliation of proprietary and budgetary information to assist users in understanding the relationship of the data. Due to the limitations of the Army General Fund financial systems, budgetary data do not agree with proprietary expenses and capitalized assets. The Army could not reconcile the information reported in Note 21 with the Army General Fund Statement of Net Cost without preparing \$9.6 billion in unsupported adjustments. The Army stated that the target date for correcting this material weakness is the third quarter of FY 2014.

#### **Contingency Payment Audit Trails**

The Army acknowledged that the maintenance of substantiating documents by certifying and entitlement activities creates significant challenges in tracing audit trails for support of financial statements. DoD Inspector General Report No. D-2008-098, "Internal Controls Over Payments Made in Iraq, Kuwait and Egypt," May 22, 2008, reported that the Army made \$1.4 billion in commercial payments that lacked the minimum supporting documentation and information for a valid payment (minimum support would include such documents as certified vouchers, proper receiving reports, and invoices). In addition, the Army estimated that \$6.3 billion of commercial payments contained the minimum supporting documentation but did not comply with other statutory and regulatory requirements. Payments that are not properly supported do not provide the necessary assurance that funds were used as intended.

DoD Inspector General Report No. D-2011-101, "Controls over Army Deployable Disbursing System Payments Need Improvement," August 17, 2011, further supports the conclusion that payment audit trails continue to be a weakness. Specifically, the Deployable Disbursing System did not maintain accurate lines of accounting information, accurate payment method information, or complete fundamental payment information, such as invoice line item information, contract or requisition numbers, and invoice numbers. Without accurate and complete data, DoD cannot maintain complete and documented audit trails, and DoD is at increased risk for improper payments. The Army stated that the target date for correcting this material weakness is the first quarter of FY 2013.



## **Previously Identified Significant Deficiencies**

As part of our financial-related audits, we noted the following significant deficiency, which continued to exist.

### **Legal Representation Process**

The Army legal representation process did not provide meaningful assessments of potential liabilities and was not linked to the Army process for reporting and disclosing contingent legal liabilities on the financial statements. This financial management deficiency may cause inaccurate management information. As a result, Army General Fund management decisions based in whole or in part on this information may be adversely affected. DoD financial information may also contain misstatements resulting from this deficiency.

These financial management deficiencies may cause inaccurate management information. As a result, DoD management decisions based in whole or in part on this information may be adversely affected. DoD reported that financial information may also contain misstatements resulting from these deficiencies.

## **Compliance with Laws and Regulations**

Management is responsible for compliance with existing laws and regulations related to financial reporting. We limited our work to determining compliance with selected provisions of the applicable laws and regulations because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Army was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on compliance with applicable laws and regulations.

### ***Federal Financial Management Improvement Act of 1996***

FFMIA requires DoD to establish and maintain financial management systems that comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level.

For FY 2012, the Army did not fully comply with FFMIA. The Deputy Assistant Secretary of the Army (Financial Operations) acknowledged that many of its critical financial management and feeder systems did not substantially comply with the Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2012.

### ***Government Performance and Results Act of 1993***

Congress enacted GPRA to establish strategic planning and performance measurement in the Federal Government. Strategic plans, annual performance plans, and annual program performance reports are the main elements of GPRA. The financial information contained in the Statement of Net Cost is not presented by programs that align with major goals and outputs described in the DoD strategic and performance plans required by GPRA. Because financial processes and systems do not correlate costs with performance measures, revenues and expenses are reported by appropriation categories. The Army did not comply with GPRA because it did not have cost accounting systems in place to collect, process, and report operating costs. This resulted in the Army being unable to present cost-of-operations data on the Army General Fund Statement of Net Cost that were consistent with the GPRA goals and measures.

### ***Antideficiency Act***

Section 1341, title 31, United States Code (31 U.S.C. § 1341) limits the Army and its agents to making or authorizing expenditures or obligations that do not exceed the available appropriations or funds. Additionally, the Army or its agents may not contract or obligate for the payment of money before an appropriation is made available for that contract or obligation unless otherwise authorized by law. According to 31 U.S.C. § 1351, if an officer or employee of an executive agency violates the Antideficiency Act (ADA), the head of the agency must report immediately to the President and Congress all relevant facts and a statement of actions taken. During FY 2012, the Army reported seven ADA violations. Therefore, the Army did not comply with 31 U.S.C. §§ 1341.

DoD 7000.14-R, "Financial Management Regulation," volume 14, chapter 7, "Antideficiency Act Report," November 2010, limits the time from identification to reporting of ADA violations to 15 months. The Army did not close five of the seven ADA violations within 15 months.

## **Audit Disclosures**

The Deputy Assistant Secretary of the Army (Financial Operations) acknowledged to us on March 30, 2012, that the Army General Fund financial management and feeder systems could not provide adequate evidence supporting various material amounts on the financial statements and that previously identified material weaknesses continued to exist. Therefore, we did not perform detailed testing related to previously identified material weaknesses. In addition, we did not perform audit work related to the following selected provisions of laws and regulations: Federal Credit Reform Act of 1990, Pay and Allowance System for Civilian Employees, Prompt Payment Act, Improper Payments Information Act, and Provisions Governing Claims of the United States (including provisions of the Debt Collection Improvement Act of 1996).

## **Recommendations**

This report does not include recommendations to correct the material weaknesses and instances of noncompliance with laws and regulations because previous audit reports contained recommendations for corrective actions or because audit projects currently in process will include appropriate recommendations.

## Department of the Army Comments



**DEPARTMENT OF THE ARMY**  
OFFICE OF THE ASSISTANT SECRETARY OF THE ARMY  
FINANCIAL MANAGEMENT AND COMPTROLLER  
109 ARMY PENTAGON  
WASHINGTON DC 20310-0109

7 November 2012

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDITING,  
DEPARTMENT OF DEFENSE

SUBJECT: Management Response to the Fiscal Year 2012 Army General Fund Financial  
Statement Audit Report

1. Please accept our thanks for your efforts on behalf of Army. We appreciate the professionalism exhibited by your staff during the audit and the opportunity to comment on the draft reports provided to us on November 5, 2012.
2. We generally concur with the findings identified in the draft Report on Internal Control. We will begin corrective actions regarding the contingency payment audit trails material weakness, which has a current target date of 1st Quarter, FY 2013. We will follow up with the US Army Audit Agency to determine whether it can validate that the Army has implemented recommendations from three previous audit reports conducted in fiscal years (FY) 2009, 2010, and 2011.
3. Regarding the accounting adjustments material weakness, the Army has fully deployed the General Fund Enterprise Business System (GFEBS) which will enable the Army to submit a General Fund trial balance directly to the Defense Finance and Accounting Service (DFAS) using the Standard Financial Information Structure. This functionality will reduce the number of unsupported accounting adjustments that DFAS needs to process. This material weakness has a target date for correction of 2nd Quarter, FY 2013.
4. Regarding abnormal account balances, the deployment of GFEBS enables the Army to detect and correct abnormal balances through routine general ledger tie point reconciliations and other processes. This material weakness has a target date for correction of 2nd Quarter, FY 2013.
5. My point of contact for this action is [REDACTED] [REDACTED] can be reached by telephone at [REDACTED] [REDACTED], or by e-mail at [REDACTED]

A handwritten signature in black ink, appearing to read "James J. Watkins".

James J. Watkins  
Deputy Assistant Secretary Army  
(Financial Operations)



## LIMITATIONS

### *Limitations of the Financial Statements*

The financial statements have been prepared to report the financial position and results of operations for the entity, pursuant to the requirements of Title 31, United States Code, Section 3515(b).

While the statements have been prepared from the books and records of the entity, in accordance with the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity.

BUILDING ON A FOUNDATION OF  
**STRENGTH**

Fiscal Year 2012 United States Army Annual Financial Report

Department of Defense - Army Working Capital Fund

**CONSOLIDATED BALANCE SHEET**

As of September 30, 2012 and 2011 (Amounts in thousands)

	2012 Consolidated	2011 Consolidated
<b>ASSETS (Note 2)</b>		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	\$ 1,334,455	\$ 1,900,483
Accounts Receivable (Note 5)	294,764	424,667
Other Assets (Note 6)	0	22,519
Total Intragovernmental Assets	\$ 1,629,219	\$ 2,347,669
Accounts Receivable, Net (Note 5)	24,233	15,684
Inventory and Related Property, Net (Note 9)	22,096,521	25,211,515
General Property, Plant and Equipment, Net (Note 10)	1,748,773	1,564,390
Other Assets (Note 6)	307,744	446,028
<b>TOTAL ASSETS</b>	<b>\$ 25,806,490</b>	<b>\$ 29,585,286</b>
<b>STEWARDSHIP PROPERTY, PLANT &amp; EQUIPMENT (Note 10)</b>		
<b>LIABILITIES (Note 11)</b>		
Intragovernmental:		
Accounts Payable (Note 12)	\$ 109,060	\$ 125,110
Other Liabilities (Note 15 & 16)	88,239	85,997
Total Intragovernmental Liabilities	\$ 197,299	\$ 211,107
Accounts Payable (Note 12)	392,970	658,288
Military Retirement and Other Federal	215,104	221,632
Employment Benefits (Note 17)		
Other Liabilities (Note 15 and Note 16)	439,834	558,526
<b>TOTAL LIABILITIES</b>	<b>\$ 1,245,207</b>	<b>\$ 1,649,553</b>
<b>COMMITMENTS AND CONTINGENCIES (NOTE 16)</b>		
<b>NET POSITION</b>		
Unexpended Appropriations - Other Funds	\$ 127,825	\$ 0
Cumulative Results of Operations - Other Funds	24,433,458	27,935,733
<b>TOTAL NET POSITION</b>	<b>\$ 24,561,283</b>	<b>\$ 27,935,733</b>
<b>TOTAL LIABILITIES AND NET POSITION</b>	<b>\$ 25,806,490</b>	<b>\$ 29,585,286</b>

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.

*Department of Defense - Army Working Capital Fund***CONSOLIDATED STATEMENT OF NET COST***As of September 30, 2012 and 2011 (Amounts in thousands)*

	2012 Consolidated	2011 Consolidated
<b>Program Costs</b>		
Gross Costs	\$ 33,365,902	\$ 29,629,581
Operations, Readiness & Support	\$ 33,365,902	\$ 29,629,581
(Less: Earned Revenue)	(30,792,842)	(33,261,795)
Net Cost before Losses/(Gains) from Actuarial Assumption		
Changes for Military Retirement Benefits	\$ 2,573,060	\$ (3,632,214)
Net Program Costs Including Assumption Changes	\$ 2,573,060	\$ (3,632,214)
<b>Net Cost of Operations</b>	<u>\$ 2,573,060</u>	<u>\$ (3,632,214)</u>

*The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.*



Department of Defense - Army Working Capital Fund

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION***As of September 30, 2012 (Amounts in thousands)*

	2012 Earmarked Funds	2012 All Other Funds	2012 Eliminations	2012 Consolidated
<b>CUMULATIVE RESULTS OF OPERATIONS</b>				
<b>Beginning Balances</b>	\$ 0	\$ 27,935,733	\$ 0	\$ 27,935,733
<b>Beginning balances, as adjusted</b>	\$ 0	\$ 27,935,733	\$ 0	\$ 27,935,733
<b>Budgetary Financing Sources:</b>				
Appropriations used	0	27,369	0	27,369
Transfers-in/out without reimbursement	0	(1,140,194)	0	(1,140,194)
<b>Other Financing Sources:</b>				
Transfers-in/out without reimbursement (+/-)	0	(91,948)	0	(91,948)
Imputed financing from costs absorbed by others	0	178,843	0	178,843
Other (+/-)	0	96,715	0	96,715
<b>Total Financing Sources</b>	\$ 0	\$ (929,215)	\$ 0	\$ (929,215)
<b>Net Cost of Operations (+/-)</b>	0	2,573,060	0	2,573,060
<b>Net Change</b>	\$ 0	\$ (3,502,275)	\$ 0	\$ (3,502,275)
<b>Cumulative Results of Operations</b>	\$ 0	\$ 24,433,458	\$ 0	\$ 24,433,458
<b>UNEXPENDED APPROPRIATIONS</b>				
<b>Budgetary Financing Sources:</b>				
Appropriations received	\$ 0	\$ 155,194	\$ 0	\$ 155,194
Appropriations used	0	(27,369)	0	(27,369)
<b>Total Budgetary Financing Sources</b>	\$ 0	\$ 127,825	\$ 0	\$ 127,825
<b>Unexpended Appropriations</b>	\$ 0	\$ 127,825	\$ 0	\$ 127,825
<b>Net Position</b>	\$ 0	\$ 24,561,283	\$ 0	\$ 24,561,283

*The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.*

Department of Defense - Army Working Capital Fund

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**

<i>As of September 30, 2012 (Amounts in thousands)</i>	2011 Earmarked Funds		2011 All Other Funds		2011 Eliminations		2011 Consolidated	
<b>CUMULATIVE RESULTS OF OPERATIONS</b>								
<b>Beginning Balances</b>	\$	0	\$	25,074,279	\$	0	\$	25,074,279
<b>Beginning balances, as adjusted</b>	\$	0	\$	25,074,279	\$	0	\$	25,074,279
<b>Budgetary Financing Sources:</b>								
Appropriations used		0		54,636		0		54,636
Transfers-in/out without reimbursement		0		(700,000)		0		(700,000)
<b>Other Financing Sources:</b>								
Transfers-in/out without reimbursement (+/-)		0		(394,625)		0		(394,625)
Imputed financing from costs absorbed by others		0		208,360		0		208,360
Other (+/-)		0		60,869		0		60,869
<b>Total Financing Sources</b>	\$	0	\$	(770,760)	\$	0	\$	(770,760)
<b>Net Cost of Operations (+/-)</b>		0		(3,632,214)		0		(3,632,214)
<b>Net Change</b>	\$	0	\$	2,861,454	\$	0	\$	2,861,454
<b>Cumulative Results of Operations</b>	\$	0	\$	27,935,733	\$	0	\$	27,935,733
<b>UNEXPENDED APPROPRIATIONS</b>								
<b>Budgetary Financing Sources:</b>								
Appropriations received	\$	0	\$	54,636	\$	0	\$	54,636
Appropriations used		0		(54,636)		0		(54,636)
<b>Total Budgetary Financing Sources</b>	\$	0	\$	0	\$	0	\$	0
<b>Unexpended Appropriations</b>	\$	0	\$	0	\$	0	\$	0
<b>Net Position</b>	\$	0	\$	27,935,733	\$	0	\$	27,935,733

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.

Department of Defense - Army Working Capital Fund

**COMBINED STATEMENT OF BUDGETARY RESOURCES**

As of September 30, 2012 and 2011 (Amounts in thousands)

As of September 30, 2012 and 2011 (Amounts in thousands)	2012 Combined		Restated 2011 Combined	
<b>BUDGETARY FINANCING ACCOUNTS</b>				
<b>BUDGETARY RESOURCES</b>				
Unobligated balance brought forward, Oct 1	\$	2,150,010	\$	1,022,350
Unobligated balance brought forward, Oct 1, as adjusted	\$	2,150,010	\$	1,022,350
Recoveries of prior year unpaid obligations		1,528,463		3,183,324
Other changes in unobligated balance (+/-)		(1,994,513)		(2,436,566)
Unobligated balance from prior year budget authority, net	\$	1,683,960	\$	1,769,108
Appropriations (discretionary and mandatory)		155,194		0
Contract authority (discretionary and mandatory)		5,979,778		8,598,144
Spending authority from offsetting collections (discretionary and mandatory)		5,382,359		6,731,182
<b>Total Budgetary Resources</b>	<b>\$</b>	<b>13,201,291</b>	<b>\$</b>	<b>17,098,434</b>
<b>STATUS OF BUDGETARY RESOURCES</b>				
Obligations incurred				
Unobligated balance, end of year	\$	12,766,482	\$	14,948,424
Apportioned		434,809		2,150,010
Total unobligated balance, end of year	\$	434,809	\$	2,150,010
<b>Total Budgetary Resources</b>	<b>\$</b>	<b>13,201,291</b>	<b>\$</b>	<b>17,098,434</b>
<b>Change in Obligated Balance</b>				
Unpaid obligations, brought forward, October 1 (gross)	\$	8,229,298	\$	9,468,963
Uncollected customer payments from federal sources, brought forward, October 1 (-)		(7,077,240)		(5,374,558)
Obligated balance start of year (net), before adjustments (+/-)		1,152,058		4,094,405
Obligated balance, start of year (net), as adjusted	\$	1,152,058	\$	4,094,405
Obligations incurred		12,766,482		14,948,424
Outlays (gross) (-)		(12,478,188)		(13,004,763)
Change in uncollected customer payments from federal sources (+/-)		1,000,241		(1,702,683)
Recoveries of prior year unpaid obligations (-)		(1,528,463)		(3,183,324)
Subtotal	\$	912,130	\$	1,152,059
Obligated balance, end of year				
Unpaid obligations, end of year (gross)		6,989,129		8,229,300
Uncollected customer payments from federal sources, end of year (-)		(6,076,999)		(7,077,241)
<b>Obligated balance, end of year</b>	<b>\$</b>	<b>912,130</b>	<b>\$</b>	<b>1,152,059</b>
<b>Budget Authority and Outlays, Net</b>				
Budget authority, gross (discretionary and mandatory)	\$	11,517,331	\$	15,329,326
Actual offsetting collections (discretionary and mandatory) (-)		(12,897,161)		(13,742,529)
Change in uncollected customer payments from federal sources (discretionary and mandatory) (+/-)		1,000,241		(1,702,683)
Budget authority, net (discretionary and mandatory)	\$	(379,589)	\$	(115,886)
Outlays, gross (discretionary and mandatory)	\$	12,478,188	\$	13,004,763
Actual offsetting collections (discretionary and mandatory) (-)		(12,897,161)		(13,742,529)
Outlays, net (discretionary and mandatory)		(418,973)		(737,766)
<b>Agency Outlays, Net (Discretionary and Mandatory)</b>	<b>\$</b>	<b>(418,973)</b>	<b>\$</b>	<b>(737,766)</b>

The accompanying notes are an integral part of these financial statements. Amounts may not sum due to rounding.

## NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

### 1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Army Working Capital Fund (WCF), as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the Army WCF in accordance with, and to the extent possible, U.S. generally accepted accounting principles (USGAAP) promulgated by the Federal Accounting Standards Advisory Board; the Office of Management and Budget (OMB) Circular No. A-136, Financial Reporting Requirements; and the Department of Defense (DoD) Financial Management Regulation. The accompanying financial statements account for all resources for which the Army WCF is responsible unless otherwise noted.

The Army WCF is unable to fully implement all elements of USGAAP and the OMB Circular No. A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. Although the Army WCF now derives most reported values and information for major asset and liability categories from the Logistics Modernization Program (LMP) system, LMP contains some system and posting deficiencies related to items such as source-accepted procurements, budgetary transactions, continuing resolutions, cash balances, and undeposited collections. In addition, LMP relies on some data from systems such as entitlement systems and property systems that compromise the ability to fully meet all USGAAP standards. The Army WCF continues to implement process and system improvements addressing these limitations. The Army WCF will continue to use generally accepted accounting principles to address functionality and processes for items such as constructive receipts, funds certification, outgoing military interdepartmental procurement requests (MIPR), and compensating controls for off-line systems.

The Army WCF currently has ten auditor identified financial statement material weaknesses: (1) Financial Management Systems; (2) Inventory; (3) General Property, Plant and Equipment; (4) Accounts Payable; (5) Statement of Net Cost; (6) Intragovernmental Eliminations; (7) Accounting Adjustments; (8) Reconciliation of Net Cost of Operations to Budget; (9) Abnormal Account Balances and (10) Statement of Budgetary Resources.

### 1.B. Mission of the Reporting Entity

The Army WCF is part of the Defense Working Capital Fund and is divided into two separate business areas: Supply Management and Industrial Operations. These business areas ensure delivery of critical items, such as petroleum products, repair parts, consumable supplies, depot maintenance services, munitions, and weapons to support the deployment and projection of lethal force as required by the nation.

### 1.C. Appropriations and Funds

Working capital funds receive funding to establish an initial corpus through an appropriation or a transfer of resources from existing appropriations or funds. The corpus finances operations and transactions that flow through the fund. A working capital fund maintains the corpus by selling goods and services to customers on a reimbursable basis. Reimbursable receipts fund future operations and generally are available in their entirety for use without further congressional action. At various times, the Congress provides additional appropriations as an infusion of cash when revenues are inadequate to cover costs within the corpus.

The Army WCF receives appropriations and funds as defense working capital (revolving) funds and uses the appropriation and funds to execute its mission and subsequently report on resource usage.

### 1.D. Basis of Accounting

The Army WCF's financial management systems are unable to meet all full accrual accounting requirements. Some of the Army WCF's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of USGAAP. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by USGAAP.

The financial statements are compiled from the underlying financial data and trial balances of the Army WCF sub-entities. The underlying data is partially derived from budgetary transactions (obligations, disbursements, and collections), reported on budgetary status reports and accruals made from nonfinancial feeder systems such as Mechanization of Contract Administrative Services System, the Defense Payroll System, and from Federal Employees' Compensation Act (FECA) liabilities.

Some of the sub-entity level trial balances may reflect known abnormal balances resulting largely from business and system processes. At the consolidated Army WCF level, these abnormal balances may not be evident. Disclosures of abnormal balances are made in the applicable footnotes, but only to the extent that the abnormal balances are evident at the consolidated level.

The DoD is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with USGAAP. One such action is the current revision of accounting systems to record transactions based on the United States Standard General Ledger (USSGL). The Army has implemented the LMP at all of the Army Materiel Command's activities except for Non-Army Managed Items (NAMI) and the U.S. Army Medical Material Agency, which is expected to transition to Operation and Maintenance, Army funding in FY 2013. The NAMI will transition to LMP in July 2014. Until LMP functionality is fully implemented, and all of the processes are updated to collect and report financial information as required by USGAAP, some of the Army WCF's financial data will be derived from a combination of budgetary transactions, nonfinancial feeder systems, and accruals.

## **1.E. Revenues and Other Financing Sources**

The Army WCF industrial operations activities recognize revenue according to the percentage-of-completion method. Supply management activities recognize revenue when an inventory item is sold.

## **1.F. Recognition of Expenses**

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. The Army WCF now derives the majority of its reported data from LMP which is designed to collect and record financial information for accruals. However, estimates are made for some major items such as payroll expenses, entitlement systems accruals, unbilled revenue, transportation expenses and MIPRs. The Army WCF continues to implement process and system improvements to address these limitations.

## **1.G. Accounting for Intragovernmental Activities**

Accounting standards require that an entity eliminates intraentity activity and balances from consolidated financial statements in order to prevent overstatement for business with itself. However, the Army WCF cannot accurately identify intragovernmental transactions by customer because LMP does not capture the correct buyer and seller data at the transaction level.

Generally, seller entities within the DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances and are then eliminated. The LMP is implementing a standard financial information structure in FY 2013 that will incorporate the necessary elements that will enable the Army WCF to correctly report, reconcile, and eliminate intragovernmental balances.

The Treasury Financial Manual Part 2 – Chapter 4700, *Agency Reporting Requirements for the Financial Report of the United States Government*, and related appendices, provide guidance for reporting and reconciling intragovernmental balances. While the Army WCF is unable to fully reconcile intragovernmental transactions with all federal agencies, the Army WCF is able to reconcile balances pertaining to FECA transactions with the Department of Labor and benefit program transactions with the Office of Personnel Management.

The DoD's proportionate share of public debt and related expenses of the federal government is not included. The federal government does not apportion debt and its related costs to federal agencies. The DoD's financial statements do not report any public debt, interest or source of public financing, whether from issuance of debt or tax revenues.

Generally, financing for the construction of DoD facilities is obtained through appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the U.S. Treasury does not allocate such costs to DoD.

## 1.H. Transactions with Foreign Governments and International Organizations

Each year, the Army WCF sells defense articles and services to foreign governments and international organizations under the provisions of the Arms Export Control Act of 1976. Under the provisions of the Act, DoD has authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the federal government. Payment in U.S. dollars is required in advance.

## 1.I. Funds with the U.S. Treasury

The Army WCF's monetary resources are maintained in U.S. Treasury accounts. The disbursing offices of the Defense Finance and Accounting Service (DFAS), the military services, and the U.S. Army Corps of Engineers (USACE), and the financial service centers of the Department of State process the majority of the Army WCF's cash collections, disbursements, and adjustments worldwide. Each disbursing station prepares monthly reports to the U.S. Treasury on checks issued, electronic fund transfers, interagency transfers, and deposits.

In addition, DFAS sites and the USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. On a monthly basis, Army WCF's FBWT is adjusted to agree with the U.S. Treasury accounts.

## 1.J. Cash and Other Monetary Assets

Not applicable.

## 1.K. Accounts Receivable

Accounts receivable from other federal entities or the public include accounts receivable, claims receivable, and refunds receivable. The allowance for uncollectible accounts due to the public is based upon an analysis of collection experience grouped by age categories. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual.

## 1.L. Direct Loans and Loan Guarantees

Not applicable.

## 1.M. Inventories and Related Property

The Army WCF has transitioned approximately 94 percent of its resale inventory to LMP which includes moving average cost (MAC) functionality. However, the on-hand, transitioned balances were not properly baselined to MAC. Accordingly, the Army WCF cannot confirm the actual historical cost of this inventory and recognizes that a portion may not be compliant with Statement of Federal Financial Accounting Standards (SFFAS) No. 3, *Accounting for Inventory and Related Property*.

The Army WCF reports the remaining 6 percent of resale inventories representing NAMI and the United States Army Medical Materiel Agency (USAMMA) at the latest Defense Logistics Agency (DLA) price or an approximation of historical cost using latest acquisition cost (LAC) adjusted for holding gains and losses. The latest DLA price and the LAC method are used because legacy inventory systems were designed for materiel management rather than financial accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with SFFAS No. 3. Additionally, these systems cannot produce financial transactions using the USSGL, as required by the Federal Management Improvement Act of 1996 (PL 104-208). The USAMMA will transfer from the Army WCF to Operation and Maintenance, Army funding in FY 2013. The NAMI will transition to LMP and MAC valuation during FY 2014.

The Army WCF manages only military- or government-specific materiel under normal conditions. Materiel is a unique term that relates to military force management and includes items such as ships, tanks, self-propelled weapons, aircraft, etc., and related spares, repair parts, and support equipment. Items commonly used in and available from the commercial sector are not managed in



Army WCF materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The Army WCF holds materiel based on military need and support for contingencies. The DoD is currently developing a methodology to be used to account for inventory held for sale and inventory held in reserve for future sale.

The Army WCF is in agreement with SFFAS No 3, Interpretation 7, *Items Held for Remanufacture*, that inventory held for repair should be accounted for as “inventory held for remanufacture.” Inventory held for remanufacture capitalizes repair and rebuild costs, values unrepaired carcasses at cost, and provides for exchange pricing concepts for customer returns. The Army WCF is unable to comply with some of the accounting requirements for remanufacturing until such time that all LMP functionality is fully implemented and all inventory-related tasks in the Army Financial Improvement Plan have been addressed.

The Army WCF recognizes excess, obsolete, and unserviceable inventory at net realizable value of \$0 pending development of an effective means of valuing such materiel.

Contractor-acquired inventory may not be properly accounted for due to system limitation.

Inventory available and purchased for resale includes consumable spare and repair parts and repairable items owned and managed by Army WCF. This inventory is retained to support military or national contingencies. Inventory held for repair is damaged inventory that requires repair to make it suitable for sale. Often, it is more economical to repair these items rather than to procure them. The Army WCF often relies on weapon systems and machinery no longer in production. As a result, the Army WCF supports a process that encourages the repair and rebuilding of certain items. This repair cycle is essential to maintaining a ready, mobile, and armed military force. Work in process balances include (1) costs related to the production or servicing of items, including direct materiel, labor, applied overhead; (2) the value of finished products or completed services that are yet to be placed in service; and (3) munitions in production and depot maintenance work with its associated costs incurred in the delivery of maintenance services.

## **1.N. Investments in U.S. Treasury Securities**

Not applicable.

## **1.O. General Property, Plant and Equipment**

The DoD’s general property, plant & equipment (PP&E) capitalization threshold is \$100 thousand except for real property, which is \$20 thousand. The Army WCF has fully implemented the threshold for all property.

The Army WCF capitalizes all PP&E used in the performance of its mission. These assets are capitalized as general PP&E, whether or not they meet the definition of any other PP&E category.

When it is in the best interest of the government, the Army WCF provides government property to contractors to complete contract work. The Army WCF either owns or leases such property, or it is purchased directly by the contractor for the government based on contract terms. When the value of contractor-procured general PP&E meets or exceeds the DoD capitalization threshold, federal accounting standards require that it be reported on Army WCF’s Balance Sheet.

The DoD developed policy and a reporting process for contractors with government-furnished equipment that provides appropriate general PP&E information for financial statement reporting. The DoD requires the Army WCF to maintain, in their property systems, information on all property furnished to contractors. These actions are structured to capture and report the information necessary for compliance with federal accounting standards. The Army WCF has not fully implemented this policy primarily due to system limitations.

## **1.P. Advances and Prepayments**

When advances are permitted by law, legislative action, or presidential authorization, DoD’s policy is to record advances and prepayments in accordance with USGAAP. Payments made in advance of the receipt of goods and services should be reported as an asset on the Balance Sheet. The DoD’s policy is to expense and properly classify assets when the related goods and services are received. The Army WCF has implemented this policy for advances identified as military and civil service employee pay advances, travel advances, and advances in contract feeder systems.

## 1.Q. Leases

Lease payments for the rental of equipment and operating facilities are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease), and the value equals or exceeds the current capitalization threshold, the Army WCF records the applicable asset as though purchased, with an offsetting liability, and depreciates it. The Army WCF records the asset and the liability at the lesser of the present value of the rental and other lease payments during the lease term (excluding portions representing executory costs paid to the lessor) or the asset's fair market value. The discount rate for the present value calculation is either the lessor's implicit interest rate or the government's incremental borrowing rate at the inception of the lease. The Army WCF, as the lessee, receives the use and possession of leased property; for example real estate or equipment from a lessor in exchange for a payment of funds. An operating lease does not substantially transfer all the benefits and risk of ownership. Payments for operating leases are expensed over the lease term as they become payable.

## 1.R. Other Assets

The Army WCF's other assets include credits due for returns and estimated future payments to contractors upon delivery and government acceptance of satisfactory products.

The Army WCF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, the Army WCF may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements to a contractor prior to acceptance of supplies or services by the government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include (1) advance payments, (2) performance-based payments, (3) commercial advance and interim payments, (4) progress payments based on cost, and (5) interim payments under certain cost-reimbursement contracts. It is DoD policy to record certain contract financing payments as Other Assets. The Army WCF has fully implemented this policy. Estimated future payments to contractors are offset by a contingent liability.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage- or stage-of-completion. The Defense Federal Acquisition Regulation Supplement authorizes progress payments based on a percentage- or stage-of-completion only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments based on percentage- or stage-of-completion are reported as construction-in-progress.

## 1.S. Contingencies and Other Liabilities

The SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, as amended by SFFAS No. 12, *Recognition of Contingent Liabilities Arising from Litigation*, defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible loss. The uncertainty will be resolved when one or more future events occur or fail to occur. The Army WCF recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist but there is at least a reasonable possibility of incurring a loss or additional losses. The Army WCF's risk of loss and resultant contingent liabilities arise from pending or threatened litigation or claims and assessments due to events such as aircraft, ship and vehicle accidents; medical malpractice; property or environmental damages; and contract disputes.

## 1.T. Accrued Leave

The Army WCF reports liabilities for accrued compensatory and annual leave for civilians. Sick leave for civilians is expensed as taken. The liabilities are based on current pay rates.

## 1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent the amounts of budget authority that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred.

Prior to FY 2012, the Army WCF treated appropriations as fully expended at the end of the fiscal year in which the appropriation was received. For FY 2012 year-end reporting, the Army WCF will identify and report obligations and disbursements to the original appropriation. Unobligated and unexpended amounts will be carried forward into the FY 2013 and beyond until the applicable appropriation is fully expended. In addition, functionality has been implemented in LMP during 2012 to facilitate this reporting process.

Cumulative Results of Operations represent the net difference between expenses and losses, and financing sources (including appropriations, revenue, and gains), since inception. The cumulative results of operations also include donations and transfers in and out of assets that were not reimbursed.

## **1.V. Treaties for Use of Foreign Bases**

Not applicable.

## **1.W. Undistributed Disbursements and Collections**

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to specific obligations, payables, or receivables in the source systems and those reported by the U.S. Treasury.

Supported disbursements and collections may be evidenced by the availability of corroborating documentation that would generally support the summary level adjustments made to accounts payable and accounts receivable. Unsupported disbursements and collections do not have supporting documentation for the transactions and most likely would not meet audit scrutiny. However, both supported and unsupported adjustments may have been made to the Army WCF accounts payable and accounts receivable trial balances before validating underlying transactions that established the accounts payable and accounts receivable. As a result, misstatements of reported accounts payable and accounts receivable are likely present in the Army WCF financial statements.

Due to noted material weakness in current accounting and financial feeder systems, the DoD is generally unable to determine whether undistributed disbursements and collections should be applied to federal or nonfederal accounts payables and accounts receivable at the time accounting reports are prepared. Accordingly, the DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Both supported and unsupported undistributed disbursements and collections are then applied to reduce accounts payable and accounts receivable accordingly.

## **1.X. Fiduciary Activities**

Not applicable.

## **1.Y. Military Retirement and Other Federal Employment Benefits**

Not applicable.

## **1.Z. Significant Events**

Not applicable.

## NOTE 2. NONENTITY ASSETS

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
<b>1. Intragovernmental Assets</b>		
A. Fund Balance with Treasury	\$ 0	\$ 0
B. Accounts Receivable	0	0
C. Other Assets	0	0
D. Total Intragovernmental Assets	\$ 0	\$ 0
<b>2. Nonfederal Assets</b>		
A. Cash and Other Monetary Assets	\$ 0	\$ 0
B. Accounts Receivable	1,858	0
C. Other Assets	0	0
D. Total Nonfederal Assets	\$ 1,858	\$ 0
<b>3. Total Nonentity Assets</b>	\$ 1,858	\$ 0
<b>4. Total Entity Assets</b>	\$ 25,804,632	\$ 29,585,286
<b>5. Total Assets</b>	\$ 25,806,490	\$ 29,585,286

### Information Related to Nonentity Assets

Assets are categorized as either entity or nonentity. Entity assets consist of resources that are available for use in the operations of the entity.

Nonentity assets are assets for which the Army Working Capital Fund (WCF) maintains stewardship accountability and reporting responsibility, but are not available for the Army WCF normal operations.

These nonentity assets are for interest, penalties and administrative fees to be collected for out-of-service debts into a receipt account and then forwarded to the U.S. Treasury.

## NOTE 3. FUND BALANCE WITH TREASURY

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
<b>1. Fund Balances</b>		
A. Appropriated Funds	\$ 0	\$ 0
B. Revolving Funds	1,334,455	1,900,483
C. Trust Funds	0	0
D. Special Funds	0	0
E. Other Fund Types	0	0
<b>F. Total Fund Balances</b>	\$ 1,334,455	\$ 1,900,483
<b>2. Fund Balances Per Treasury Versus Agency</b>		
A. Fund Balance per Treasury	\$ 1,334,455	\$ 1,900,483
B. Fund Balance per Army WCF	1,334,455	1,900,483
<b>3. Reconciling Amount</b>	\$ 0	\$ 0

### Status of Fund Balance with Treasury

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
<b>1. Unobligated Balance</b>		
A. Available	\$ 434,809	\$ 2,150,010
B. Unavailable	0	0
<b>2. Obligated Balance not yet Disbursed</b>	6,989,129	8,229,300
<b>3. Nonbudgetary FBWT</b>	0	0
<b>4. NonFBWT Budgetary Accounts</b>	(6,089,483)	(8,478,827)
<b>5. Total</b>	\$ 1,334,455	\$ 1,900,483

### Information Related to Fund Balance with Treasury

The Status of Fund Balance with Treasury (FBWT) reflects the budgetary resources to support FBWT and is a reconciliation between budgetary and proprietary accounts. It primarily consists of unobligated and obligated balances. The balances reflect the budgetary authority remaining for disbursement against current or future obligations.

Unobligated Balance is classified as available or unavailable and represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. Certain unobligated balances are restricted for future use and are not apportioned for current use.

Obligated Balance not yet Disbursed represents funds that have been obligated for goods and services not received, and those received but not paid.

Non-FBWT Budgetary Accounts reduces the Status of FBWT. For the Army Working Capital Fund, these include unfilled orders without advances, reimbursements earned receivable, and contract authority.

## NOTE 4. INVESTMENTS AND RELATED INTEREST

Not applicable.

## NOTE 5. ACCOUNTS RECEIVABLE

As of September 30 (Amounts in thousands)	2012		
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
1. Intragovernmental Receivables	\$ 294,764	N/A	\$ 294,764
2. Nonfederal Receivables (From the Public)	39,050	\$ (14,817)	24,233
3. Total Accounts Receivable	\$ 333,814	\$ (14,817)	\$ 318,997

As of September 30 (Amounts in thousands)	2011		
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
1. Intragovernmental Receivables	\$ 424,667	N/A	\$ 424,667
2. Nonfederal Receivables (From the Public)	30,130	\$ (14,446)	15,684
3. Total Accounts Receivable	\$ 454,797	\$ (14,446)	\$ 440,351

### Information Related to Accounts Receivable

The accounts receivable represent the Army Working Capital Fund (WCF) claim for payment from other entities. The Army WCF only recognizes an allowance for uncollectible amounts from the public. Claims with other federal agencies are resolved in accordance with the Intragovernmental Business Rules.

## NOTE 6. OTHER ASSETS

As of September 30 (Amounts in thousands)	2012		2011	
1. Intragovernmental Other Assets				
A. Advances and Prepayments	\$	0	\$	3
B. Other Assets		0		22,516
C. Total Intragovernmental Other Assets	\$	0	\$	22,519
2. Nonfederal Other Assets				
A. Outstanding Contract Financing Payments	\$	307,652	\$	409,748
B. Advances and Prepayments		92		36,280
C. Other Assets (With the Public)		0		0
D. Total Nonfederal Other Assets	\$	307,744	\$	446,028
3. Total Other Assets	\$	307,744	\$	468,547

### Information Related to Other Assets

Other Assets (Intragovernmental) consist of the turn-in of unserviceable and obsolete inventory awaiting credit dispositions from federal resources, e.g., Defense Logistics Agency.

Contract terms and conditions for certain types of contract financing payments convey certain rights to the government that protect the contract work from state or local taxation, liens or attachments by the contractor's creditors, transfer of property, or disposition in bankruptcy. However, these rights should not be misconstrued to mean that ownership of the contractor's work has transferred to the federal government. The federal government does not have the right to take the work, except as provided in contract clauses related to termination or acceptance, and the Army Working Capital Fund is not obligated to make payment to the contractor until delivery and acceptance.

The balance of Outstanding Contract Financing Payments includes \$293.1 million in contract financing payments and an additional \$14.6 million in estimated future payments to contractors upon delivery and government acceptance of a satisfactory product. See additional discussion in Note 15, *Other Liabilities*.

## NOTE 7. CASH AND OTHER MONETARY ASSETS

Not Applicable.

## NOTE 8. DIRECT LOAN AND LOAN GUARANTEES

Not Applicable.

## NOTE 9. INVENTORY AND RELATED PROPERTY

As of September 30	2012		2011	
(Amounts in thousands)				
1. Inventory, Net	\$	22,096,521	\$	25,211,515
2. Operating Materiel & Supplies, Net		0		0
3. Stockpile Materiel, Net		0		0
4. Total	\$	22,096,521	\$	25,211,515

### Information Related to Inventory and Related Property

As a result of audit readiness efforts, adjustments were made to the Army Working Capital Fund's (WCF) mission critical assets. These accounting adjustments were recognized in current year cost accounts when auditable data was not available to support restatement of prior period financial statements.

### Inventory, Net

As of September 30 <i>(Amounts in thousands)</i>	2012			Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	
<b>1. Inventory Categories</b>				
A. Available and Purchased for Resale	\$ 15,739,274	\$ (1,644,253)	\$ 14,095,021	MAC, FIFO, LAC
B. Held for Repair	6,592,703	56,202	6,648,905	LAC, MAC
C. Excess, Obsolete, and Unserviceable	154,138	(154,138)	0	NRV
D. Raw Materiel	1,352,562	0	1,352,562	MAC, SP, LAC
E. Work in Process	33	0	33	AC
<b>F. Total</b>	<b>\$ 23,838,710</b>	<b>\$ (1,742,189)</b>	<b>\$ 22,096,521</b>	



**As of September 30***(Amounts in thousands)*

	<b>2011</b>			<b>Valuation Method</b>
	<b>Inventory, Gross Value</b>	<b>Revaluation Allowance</b>	<b>Inventory, Net</b>	
<b>1. Inventory Categories</b>				
A. Available and Purchased for Resale	\$ 16,571,240	\$ (224,934)	\$ 16,346,306	LAC, MAC
B. Held for Repair	7,204,345	151,630	7,355,975	LAC, MAC
C. Excess, Obsolete, and Unserviceable	313,385	(313,385)	0	NRV
D. Raw Materiel	1,373,697	0	1,373,697	MAC, SP, LAC
E. Work in Process	135,537	0	135,537	AC
<b>F. Total</b>	<b>\$ 25,598,204</b>	<b>\$ (386,689)</b>	<b>\$ 25,211,515</b>	

**Legend for Valuation Methods:**

LAC = Latest Acquisition Cost

SP = Standard Price

AC = Actual Cost

MAC = Moving Average Cost

NRV = Net Realizable Value

LCM = Lower of Cost or Market

FIFO = First In, First Out

Inventory Held for Repair Revaluation Allowance has an abnormal balance of \$56.2 million as a result of postings in the Logistics Modernization Program carried forward from the FY 2009 migration from Commodity Command Standard System. The issue is being addressed with a system change request.

There are restrictions on the use, sale, and disposition of inventory classified as war reserve materiel valued at moving average cost of \$1.2 billion which includes petroleum products, subsistence items, spare parts, and medical materiel.

The categories listed comprise Inventory, Net. The Army WCF assigns inventory items to a category based upon the type and condition of the asset. Inventory Available and Purchased for Resale includes spare and repair parts, clothing, textiles, and petroleum products. Inventory Held for Repair consists of damaged materiel held as inventory that is more economical to repair than to dispose. Excess, Obsolete, and Unserviceable Inventory consists of scrap materiel or items that cannot be economically repaired and are awaiting disposal. Raw Materiel consists of items consumed in the production of goods for sale or in the provision of services for a fee.

Work-in-Process includes costs related to producing or servicing of items, including direct material, direct labor, applied overhead and other direct costs. Work-in-Process also includes the value of the finished products or completed services pending the submission of bills to the customer. The work-in-process designation may also be used to accumulate the amount paid to the contractor under cost reimbursable contracts, including amounts withheld from payment to ensure performance, and amounts paid to other government plants for accrued costs of end items of materiel ordered but not delivered. Work-in-Process includes munitions in production and depot maintenance work and its associated labor, applied overhead, and supplies used in the delivery of maintenance services.

**Operating Materiel and Supplies, Net**

Not Applicable.

**Stockpile Materiel, Net**

Not Applicable.

## NOTE 10. GENERAL PP&E, NET

As of September 30	2012				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
<i>(Amounts in thousands)</i>					
<b>1. Major Asset Classes</b>					
A. Land	N/A	N/A	\$ 9,693	N/A	\$ 9,693
B. Buildings, Structures, and Facilities	S/L	20 or 40	2,096,918	\$ (1,514,600)	582,318
C. Leasehold Improvements	S/L	lease term	0	0	0
D. Software	S/L	2-5 or 10	1,064,497	(599,089)	465,408
E. General Equipment	S/L	5 or 10	1,645,126	(1,241,441)	403,685
F. Military Equipment	S/L	various	0	0	0
G. Shipbuilding (Construction-in-Progress)	N/A	N/A	0	0	0
H. Assets Under Capital Lease	S/L	lease term	0	0	0
I. Construction-in-Progress (excludes Military Equipment)	N/A	N/A	287,669	N/A	287,669
J. Other			0	0	0
<b>K. Total General PP&amp;E</b>			<u>\$ 5,103,903</u>	<u>\$ (3,355,130)</u>	<u>\$ 1,748,773</u>

As of September 30	2011				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
<i>(Amounts in thousands)</i>					
<b>1. Major Asset Classes</b>					
A. Land	N/A	N/A	\$ 0	N/A	\$ 0
B. Buildings, Structures, and Facilities	S/L	20 or 40	1,852,835	\$ (1,435,177)	417,658
C. Leasehold Improvements	S/L	lease term	0	0	0
D. Software	S/L	2-5 or 10	1,001,228	(473,998)	527,230
E. General Equipment	S/L	5 or 10	1,547,279	(1,212,537)	334,742
F. Military Equipment	S/L	various	0	0	0
G. Shipbuilding (Construction-in-Progress)	N/A	N/A	0	0	0
H. Assets Under Capital Lease	S/L	lease term	0	0	0
I. Construction-in-Progress (excludes Military Equipment)	N/A	N/A	284,760	N/A	284,760
J. Other			0	0	0
<b>K. Total General PP&amp;E</b>			<u>\$ 4,686,102</u>	<u>\$ (3,121,712)</u>	<u>\$ 1,564,390</u>

### Assets Under Capital Lease

Not Applicable.

## NOTE 11. LIABILITIES NOT COVERED BY BUDGETARY RESOURCES

As of September 30	2012		2011	
(Amounts in thousands)				
<b>1. Intragovernmental Liabilities</b>				
A. Accounts Payable	\$	0	\$	0
B. Debt		0		0
C. Other		60,762		63,765
D. Total Intragovernmental Liabilities	\$	60,762	\$	63,765
<b>2. Nonfederal Liabilities</b>				
A. Accounts Payable	\$	0	\$	0
B. Military Retirement and Other Federal Employment Benefits		215,104		221,632
C. Environmental Liabilities		0		0
D. Other Liabilities		2,544		0
E. Total Nonfederal Liabilities	\$	217,648	\$	221,632
<b>3. Total Liabilities Not Covered by Budgetary Resources</b>	\$	278,410	\$	285,397
<b>4. Total Liabilities Covered by Budgetary Resources</b>		966,797		1,364,156
<b>5. Total Liabilities</b>	\$	1,245,207	\$	1,649,553

### Information Related to Liabilities Not Covered by Budgetary Resources

Liabilities Not Covered by Budgetary Resources include liabilities for which congressional action is needed before budgetary resources can be provided.

Intragovernmental Other Liabilities represent future-funded Federal Employees' Compensation Act (FECA) liabilities billed to the Army Working Capital Fund by the Department of Labor (DOL) for payment made by DOL to Army beneficiaries.

Military Retirement and Other Federal Employment Benefits consists of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities primarily consist of \$215.1 million for the FECA actuarial reserve. Refer to Note 17, *Military Retirement and Other Federal Employment Benefits*, for additional details and disclosures.

Nonfederal Other Liabilities consist of material returns of non-Army managed items in the amount of \$2.5 million.

## NOTE 12. ACCOUNTS PAYABLE

As of September 30	2012			
(Amounts in thousands)	Accounts Payable		Interest, Penalties, and Administrative Fees	Total
1. Intragovernmental Payables	\$	109,060	N/A	\$ 109,060
2. Nonfederal Payables (to the Public)		392,970	\$ 0	392,970
3. Total	\$	502,030	\$ 0	\$ 502,030

As of September 30	2011			
(Amounts in thousands)	Accounts Payable		Interest, Penalties, and Administrative Fees	Total
1. Intragovernmental Payables	\$	125,110	N/A	\$ 125,110
2. Nonfederal Payables (to the Public)		658,288	\$ 0	658,288
3. Total	\$	783,398	\$ 0	\$ 783,398

### Information Related to Accounts Payable

Accounts Payable include amounts owed to federal and nonfederal entities for goods and services received by the Army Working Capital Fund (WCF). The Army WCF's systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side accounts payable are adjusted to agree with interagency seller-side accounts receivable. Accounts payable was adjusted by reclassifying amounts between federal and nonfederal accounts payable and recorded as supported undistributed.

## NOTE 13. DEBT

Not applicable.

## NOTE 14. ENVIRONMENTAL LIABILITIES AND DISPOSAL LIABILITIES

Not applicable.

## NOTE 15. OTHER LIABILITIES

As of September 30 (Amounts in thousands)	2012			2011
	Current Liability	Noncurrent Liability	Total	Total
<b>1. Intragovernmental</b>				
A. Advances from Others	\$ 5,887	\$ 0	\$ 5,887	\$ 2,543
B. Deposit Funds and Suspense Account Liabilities	0	0	0	0
C. Disbursing Officer Cash	0	0	0	0
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	18,696	42,065	60,761	63,765
F. Custodial Liabilities	1,857	0	1,857	0
G. Employer Contribution and Payroll Taxes Payable	19,734	0	19,734	19,689
H. Other Liabilities	0	0	0	0
I. Total Intragovernmental Other Liabilities	\$ 46,174	\$ 42,065	\$ 88,239	\$ 85,997
<b>2. Nonfederal</b>				
A. Accrued Funded Payroll and Benefits	\$ 217,041	\$ 0	\$ 217,041	\$ 241,428
B. Advances from Others	65,781	(1)	65,780	94,166
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	0	0	0	0
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	0	0	0	0
H. Capital Lease Liability	0	0	0	0
I. Contract Holdbacks	16,262	0	16,262	30,769
J. Employer Contribution and Payroll Taxes Payable	30,418	0	30,418	31,620
K. Contingent Liabilities	0	14,582	14,582	118,177
L. Other Liabilities	95,751	0	95,751	42,366
M. Total Nonfederal Other Liabilities	\$ 425,253	\$ 14,581	\$ 439,834	\$ 558,526
<b>3. Total Other Liabilities</b>	<b>\$ 471,427</b>	<b>\$ 56,646</b>	<b>\$ 528,073</b>	<b>\$ 644,523</b>

### Information Related to Other Liabilities

Nonfederal Other Liabilities primarily consist of \$93.2 million for industrial operations service accruals.

### Contingent Liabilities

Contingent liabilities include \$14.6 million related to contracts authorizing payments based on cost as defined in the Federal Acquisition Regulation (FAR). In accordance with contract terms, specific rights to a contractor's work vests with the federal government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contractor nonperformance. It is DoD policy that these rights not be misconstrued as rights of ownership. The Army Working Capital Fund (WCF) is under no obligation to pay contractors for amounts greater than the amounts of progress payments authorized in contracts until delivery and government acceptance. Due to the probability the contractors will complete their efforts and deliver

satisfactory products, and because the amount of contractor costs incurred but yet unpaid are estimable, the Army WCF has recognized a contingent liability for the estimated unpaid costs that are considered conditional for payment pending delivery and government acceptance.

Total contingent liabilities for progress payments based on cost represent the difference between the estimated costs incurred to date by contractors and amounts authorized to be paid under progress payments based on cost provisions within the FAR. Estimated contractor-incurred costs are calculated by dividing the cumulative unliquidated progress payments based on costs by the contractor-authorized progress payment rate. The balance of unliquidated progress payments based on cost is deducted from the estimated total contractor-incurred costs to determine the contingency amount.

### Capital Lease Liability

Not applicable.

## NOTE 16. COMMITMENTS AND CONTINGENCIES

### Information Related to Commitments and Contingencies

The Army Working Capital Fund (WCF) is a party in various administrative proceedings and legal actions related to claims for environmental damage, equal opportunity matters, and contractual bid protests. We are not aware of any contingent liabilities for legal actions.

Additionally, the Army WCF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of budgetary resources. Currently, Army WCF has limited automated system processes by which it captures or assesses these potential liabilities; therefore, the amounts reported may not fairly present Army WCF's commitments and contingencies. The Army WCF records contingent liabilities in Note 15, *Other Liabilities*.

## NOTE 17. MILITARY RETIREMENT AND OTHER FEDERAL EMPLOYMENT BENEFITS

As of September 30 (Amounts in thousands)	2012			2011
	Liabilities	(Less: Assets Available to Pay Benefits)	Unfunded Liabilities	Unfunded Liabilities
<b>1. Pension and Health Benefits</b>				
A. Military Retirement Pensions	\$ 0	\$ 0	\$ 0	\$ 0
B. Military Pre Medicare Retiree Health Benefits	0	0	0	0
C. Military Medicare-Eligible Retiree Health Benefits	0	0	0	0
D. Total Pension and Health Benefits	\$ 0	\$ 0	\$ 0	\$ 0
<b>2. Other Actuarial Benefits</b>				
A. FECA	\$ 215,104	\$ 0	\$ 215,104	\$ 221,632
B. Voluntary Separation Incentive Programs	0	0	0	0
C. DoD Education Benefits Fund	0	0	0	0
D. Other	0	0	0	0
E. Total Other Actuarial Benefits	\$ 215,104	\$ 0	\$ 215,104	\$ 221,632
<b>3. Total Military Retirement and Other Federal Employment Benefits:</b>	<u>\$ 215,104</u>	<u>\$ 0</u>	<u>\$ 215,104</u>	<u>\$ 221,632</u>

### Information Related to Military Retirement and Other Federal Employment Benefits

#### Federal Employees' Compensation Act

Actuarial liabilities are computed for employee compensation benefits as mandated by the Federal Employees' Compensation Act (FECA). The Office of Personnel Management provides updated Army actuarial liabilities during the 4th quarter of each fiscal year.

The Army Working Capital Fund (WCF) computes its portion of the total Army actuarial liability based on the percentage of Army WCF FECA expense to the total Army FECA expense.

The Army WCF actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to Army WCF at the end of each fiscal year. The liability includes the estimated liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred-but-not-reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. The projected annual benefit payments are discounted to present value using the Office of Management and Budget's (OMB) economic assumptions for 10-year Treasury notes and bonds. Cost-of-living adjustments (COLAs) and consumer price index medical (CPIM) factors are applied to the calculation of projected future benefits. The actuarial liability for FECA decreased \$6.5 million between FY 2011 and FY 2012.

The estimate for future workers' compensation (FWC) benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred-but-not-reported claims. Consistent with past practice, these projected annual benefits payments have been discounted to present value using OMB's economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

#### Discount Rates

2.293% in Year 1;

3.138% in Year 2, and thereafter

To provide more specifically for the effects of inflation on the liability for FWC benefits, COLAs and CPIMs were applied to the calculation of projected future benefits. The actual rates for the above factors applied to charge back year (CBY) 2012 were also used to adjust the historical payments to current year constant dollars.

The compensation COLAs and CPIMs used in the projections for various CBYs were as follows:

CBY	COLA	CPIM
2012	N/A	N/A
2013	2.83%	3.65%
2014	2.03%	3.66%
2015	1.93%	3.72%
2016	2.00%	3.73%
2017+	2.03%	3.80%

The model's resulting projections were analyzed to insure that the estimates were reliable. The analysis was based on four tests:

(1) a sensitivity analysis of the model to economic assumptions, (2) a comparison of the percentage change in the liability amount to the percentage change in the actual incremental payments, (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2012 to the average pattern observed during the most current three charge back years, and (4) a comparison of the estimated liability per case in the 2012 projection to the average pattern for the projections of the most recent three projections.



## NOTE 18. GENERAL DISCLOSURES RELATED TO THE STATEMENT OF NET COST

### Intragovernmental Costs and Exchange Revenue

As of September 30	2012		2011	
(Amounts in thousands)				
Operations, Readiness & Support				
1. Gross Cost				
A. Intragovernmental Cost	\$	3,136,647	\$	3,315,509
B. Nonfederal Cost		30,229,255		26,314,072
C. Total Cost	\$	33,365,902	\$	29,629,581
2. Earned Revenue				
A. Intragovernmental Revenue	\$	(14,099,933)	\$	(14,497,643)
B. Nonfederal Revenue		(16,692,909)		(18,764,152)
C. Total Revenue	\$	(30,792,842)	\$	(33,261,795)
3. Losses/(Gains) from Actuarial Assumption				
Changes for Military Retirement Benefits		0		0
4. Costs Not Assigned to Programs		0		0
5. (Less: Earned Revenues) Not Attributed to Programs		0		0
Total Net Cost	\$	2,573,060	\$	(3,632,214)

### Information Related to the Statement of Net Cost

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the federal government that are supported by appropriations or other means. The intent of the SNC is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The DoD's current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The DoD is in the process of reviewing available data and developing a cost reporting methodology as required by the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, as amended by SFFAS No. 30, *Inter-entity Cost Implementation*.

Intragovernmental costs and revenue represent transactions made between two reporting entities within the Federal Government.

Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

The Army Working Capital Fund (WCF) systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side expenses are adjusted to agree with internal seller-side revenues. Expenses were adjusted by reclassifying amounts between federal and nonfederal expenses. Intradepartmental revenues and expenses are then eliminated.

While Army WCF activities generally record transactions on an accrual basis, as is required by federal generally accepted accounting principles, the systems do not always capture actual costs. Some of the information presented on the Consolidated SNC is based on non-financial feeder systems, including property accountability and logistics systems.

## NOTE 19. DISCLOSURES RELATED TO THE STATEMENT OF CHANGES IN NET POSITION

### Information Related to the Statement of Changes in Net Position

Other Financing Sources, Other on the Statement Changes in Net Position (SCNP) consist of other gains and other losses from nonexchange activity primarily attributable to intragovernmental transfers-in or out for which trading partners could not be identified.

Appropriations Received on the SCNP do not agree with Appropriations on the Statement of Budgetary Resources for FY 2011. In FY 2011, the appropriation was recorded as a cash infusion and the appropriations used represented a liquidation of contract authority that was recorded as fully expended. During FY 2012, the appropriations received did not liquidate contract authority and are, therefore, consistent on both statements. Refer to Note 20, *Disclosures Related to the Statement of Budgetary Resources*, for additional details and disclosures.

## NOTE 20. DISCLOSURES RELATED TO THE STATEMENT OF BUDGETARY RESOURCES

As of September 30	2012	2011
<i>(Amounts in thousands)</i>		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 6,087,248	\$ 7,452,394
2. Available Borrowing and Contract Authority at the End of the Period	\$ 0	\$ 0

### Information Related to the Statement of Budgetary Resources

Allotments - Realized Resources have an abnormal balance of \$5.0 billion on the consolidated trial balance as a result of legacy system migration issues and current Logistics Modernization Program posting logic. Research is being performed to resolve this issue by the end of 1st Quarter, FY 2013.

The Army Working Capital Fund (WCF) obligations represent reimbursable obligations of \$12.7 billion and direct obligations of \$27.4 million in apportionment category B, apportioned by project or activity.

The Army WCF Statement of Budgetary Resources (SBR) includes intraentity transactions because the statements are presented as combined.

There are no legal arrangements affecting the use of unobligated balances of budgetary authority.

The Army WCF received appropriations in FY 2012 in the amount of \$155.2 million to fund war reserve materiel.

During FY 2012, the appropriations received did not liquidate contract authority and were, therefore, consistent on both statements. For FY 2011, appropriations on the SBR did not agree with Appropriations Received on the Statement of Changes in Net Position. The appropriation was recorded as a cash infusion and the appropriations used represented a liquidation of contract authority that was recorded as fully expended.

Additionally, the SBR was revised during FY 2012 and now displays spending and appropriation authority, net of any contract authority substitutions or liquidations. Accordingly, the Appropriations and Spending Authority balances in the prior year column do not correspond with the prior year published statements. For FY 2011, appropriations received and spending authority realized, before any liquidations or substitutions, were \$54.6 million and \$15.4 billion, respectively.

**NOTE 21. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET**

As of September 30	2012		2011	
(Amounts in thousands)				
<b>Resources Used to Finance Activities:</b>				
Budgetary Resources Obligated:				
1. Obligations incurred	\$	12,766,482	\$	14,948,424
2. Less: Spending authority from offsetting collections and recoveries (-)		(13,425,383)		(18,628,537)
3. Obligations net of offsetting collections and recoveries	\$	(658,901)	\$	(3,680,113)
4. Less: Offsetting receipts (-)		0		0
5. Net obligations	\$	(658,901)	\$	(3,680,113)
Other Resources:				
6. Donations and forfeitures of property	\$	0	\$	0
7. Transfers in/out without reimbursement (+/-)		(91,948)		(394,625)
8. Imputed financing from costs absorbed by others		178,843		208,360
9. Other (+/-)		96,715		60,869
10. Net other resources used to finance activities	\$	183,610	\$	(125,396)
11. Total resources used to finance activities	\$	(475,291)	\$	(3,805,509)
<b>Resources Used to Finance Items Not Part of the Net Cost of Operations:</b>				
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:				
12a. Undelivered Orders (-)	\$	1,365,146	\$	1,694,505
12b. Unfilled Customer Orders		(976,031)		1,611,879
13. Resources that fund expenses recognized in prior periods (-)		(9,532)		0
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations		0		0
15. Resources that finance the acquisition of assets (-)		(4,395,874)		(7,249,639)
16. Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations:				
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)		0		0
16b. Other (+/-)		(4,767)		333,756
17. Total resources used to finance items not part of the Net Cost of Operations	\$	(4,021,058)	\$	(3,609,499)
18. Total resources used to finance the Net Cost of Operations	\$	(4,496,349)	\$	(7,415,008)

As of September 30	2012		2011	
(Amounts in thousands)				
<b>Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period</b>				
<b>Components Requiring or Generating Resources in Future Period:</b>				
19. Increase in annual leave liability	\$	0	\$	0
20. Increase in environmental and disposal liability		0		0
21. Upward/Downward reestimates of credit subsidy expense (+/-)		0		0
22. Increase in exchange revenue receivable from the public (-)		0		0
23. Other (+/-)		2,544		19,857
24. Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	\$	2,544	\$	19,857
<b>Components Not Requiring or Generating Resources:</b>				
25. Depreciation and amortization	\$	255,811	\$	214,143
26. Revaluation of assets or liabilities (+/-)		(833,774)		(3,562,869)
27. Other (+/-)				
27a. Trust Fund Exchange Revenue		0		0
27b. Cost of Goods Sold		14,113,747		12,758,695
27c. Operating Material and Supplies Used		0		0
27d. Other		(6,468,919)		(5,647,032)
28. Total Components of Net Cost of Operations That Will Not Require or Generate Resources	\$	7,066,865	\$	3,762,937
29. Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period		7,069,409		3,782,794
<b>30. Net Cost of Operations</b>	\$	2,573,060	\$	(3,632,214)

### Information Related to the Reconciliation of Net Cost of Operations to Budget

Due to Army Working Capital Fund's financial systems limitations, budgetary data do not agree with proprietary expenses and capitalized assets. The difference between budgetary and proprietary data is a previously identified deficiency.

Resources that finance the acquisition of assets were adjusted by a net of \$214.1 million to bring the note schedule into agreement with the Statement of Net Cost.

Reconciliation of net cost of operations to budget lines are presented as combined instead of consolidated due to intraagency budgetary transactions not being eliminated:

- Obligations Incurred
- Less: Spending Authority from Offsetting Collections and Recoveries
- Obligations Net of Offsetting Collections and Recoveries
- Less: Offsetting Receipts
- Net Obligations
- Undelivered Orders
- Unfilled Customer Orders

Other Resources, Other consist of other gains and other losses from non exchange activity primarily attributable to intragovernmental transfers-in/out for which trading partners could not be identified.

Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations, Other consist of other gains and losses from nonexchange activity primarily attributable to intragovernmental transfers-in or out for which trading partners could not be identified and the correction of prior-period adjustments that did not meet the materiality thresholds.

Components Requiring or Generating Resources in Future Period, Other consist of FECA expense.

Components Not Requiring or Generating Resources, Other consist of cost capitalization offsets. Agencies must first record all expenses to Operating Expenses/Program Costs. These expenses are then offset using the Cost Capitalization Offset account when the costs are capitalized to the appropriate “in-process type” account.

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## **NOTE 22.DISCLOSURES RELATED TO INCIDENTAL CUSTODIAL COLLECTIONS**

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Not applicable.

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## **NOTE 23.EARMARKED FUNDS**

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Not applicable.

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## **NOTE 24.FIDUCIARY ACTIVITIES**

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Not applicable.

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## **NOTE 25.OTHER DISCLOSURES**

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Not applicable.

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## **NOTE 26.RESTATEMENTS**

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Not applicable.



**INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
4800 MARK CENTER DRIVE  
ALEXANDRIA, VIRGINIA 22350-1500**

November 8, 2012

MEMORANDUM FOR ASSISTANT SECRETARY OF THE ARMY (FINANCIAL MANAGEMENT AND COMPTROLLER)

SUBJECT: Independent Auditor's Report on the Army Working Capital Fund FY 2012 and FY 2011 Financial Statements  
(Report No. DODIG-2013-011)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Army Working Capital Fund Consolidated Balance Sheet as of September 30, 2012 and 2011, and the Consolidated Statement of Net Cost, Consolidated Statement of Changes in Net Position, Combined Statement of Budgetary Resources, and related notes for the fiscal years then ended. The financial statements are the responsibility of Army management. Management is also responsible for implementing effective internal control and for complying with laws and regulations. In addition, management is responsible for implementing and maintaining financial management systems that comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA). Our responsibility is to express an opinion on the financial statements based on our audit.

We are unable to express an opinion on the Army Working Capital Fund FY 2012 and FY 2011 Basic Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer, we are including the required report on Internal Control and Compliance with Laws and Regulations. This report is an integral part of our opinion report on the financial statements and should be considered in assessing the results of our work.

### **Disclaimer of Opinion on the Financial Statements**

The Deputy Assistant Secretary of the Army (Financial Operations) represented to us that the Army Working Capital Fund FY 2012 and FY 2011 Annual Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (U.S. GAAP) and that Army financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2012. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted auditing standards that are consistent with the management representations made to us. Accordingly, we did not perform all the auditing procedures required by generally accepted government auditing standards and Office of Management and Budget (OMB) Bulletin 07-04, "Audit Requirements for Federal Financial Statements," September 4, 2007, as amended,<sup>1</sup> to determine whether material amounts on the financial statements were presented fairly.

Prior audits have identified, and Army management has also acknowledged, the long-standing material internal control weaknesses identified in the Summary of Internal Control. These material internal control weaknesses may affect the reliability of certain information contained in the annual financial statements – much of which is taken from the same data sources.<sup>2</sup> Therefore, we are unable to express, and we do not express, an opinion on the Basic Financial Statements.

<sup>1</sup> OMB Memorandum M-09-33, Technical Amendments to OMB Bulletin No. 07-04, "Audit Requirements for Federal Financial Statements," September 23, 2009.

<sup>2</sup> The annual financial statements include the basic statements, Management Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.



## Summary of Internal Control

In planning our work, we considered Army Working Capital Fund internal control over financial reporting and compliance with applicable laws and regulations. We did this to determine our audit procedures and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations. However, previously identified significant deficiencies, all of which are material, continue to exist in the following areas:

- Financial Management Systems
- Inventory
- General Property, Plant, and Equipment
- Accounts Payable
- Abnormal Account Balances
- Statement of Net Cost
- Statement of Budgetary Resources
- Intragovernmental Eliminations
- Other Accounting Entries
- Reconciliation of Net Cost of Operations to Budget

A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis.<sup>3</sup>

Internal control work we conducted as part of our prior audits would not necessarily disclose all deficiencies. Attachment 1 offers additional details on significant deficiencies, all of which we consider to be material weaknesses.

The Army reported these 10 material weaknesses in its FY 2012 Statement of Assurance.

## Compliance with Laws and Regulations

We limited our work to determining compliance with selected provisions of applicable laws and regulations related to financial reporting because management represented that instances of noncompliance identified in prior audits continue to exist. The Deputy Assistant Secretary of the Army (Financial Operations) represented to us that Army financial management systems do not substantially comply with Federal financial management systems requirements, U.S. GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether the Army Working Capital Fund complied with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See Attachment 1 for additional details on compliance with laws and regulations.

## Other Information in the Annual Financial Statements

The Army Working Capital Fund Management Discussion and Analysis and Required Supplementary Information are not a required part of the basic financial statements, and we did not audit and do not express an opinion on such information. However, we have applied certain limited procedures prescribed by auditing standards that raised doubts that we were unable to resolve regarding whether material modifications should be made to the information for it to conform with U.S. GAAP. We compared the information with the Army Working Capital Fund financial statements for consistency. Based on our limited work, we found inconsistencies between the information and the financial statements and applicable sections of OMB Circular No. A 136 (Revised), "Financial Reporting Requirements," August 3, 2012, and DoD 7000.14 R, "Financial Management Regulation," volume 6B, "Form and Content of DoD Audited Financial Statements," June 2012.

<sup>3</sup> A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a deficiency or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

## Scope and Methodology

Management is responsible for:

- preparing financial statements that conform with U.S. GAAP;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) are met;
- ensuring that the Army Working Capital Fund financial management systems substantially comply with FFMIA requirements; and
- complying with applicable laws and regulations.

We are responsible for planning and performing the audit to obtain reasonable assurance and to provide an opinion on whether the Army Working Capital Fund financial statements are presented fairly, in all material respects, in conformity with U.S. GAAP. We are also responsible for (1) testing whether Army financial management systems substantially comply with the three FFMIA requirements, (2) testing compliance with selected provisions of laws and regulations that have direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and (3) performing limited procedures with respect to certain other information appearing in the annual financial statements.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing over financial reporting and compliance to previously identified significant deficiencies, all of which are material and continue to exist. Because of inherent limitations in internal controls, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected.

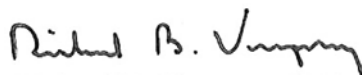
Because of the significance of the limitations on the scope of our work, we were unable to and did not perform our audit of internal control in accordance with U.S. GAAP and OMB audit guidance. We considered the limitation on the scope of our work in forming conclusions and in testing the financial statements.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

## Agency Comments and Our Evaluation

On November 5, 2012, we provided a draft of this report to the Deputy Assistant Secretary of the Army (Financial Operations). The Deputy Assistant Secretary of the Army (Financial Operations) responded in a memorandum dated November 7, 2012, which is included in its entirety at Attachment 2. The Department's response was considered in preparing the final version of this report.

This report is intended solely for the information and use of the Department's management, DoD Office of Inspector General, OMB, Government Accountability Office, and Congress and is not intended to be used by anyone other than these specified parties.



Richard B. Vasquez, CPA  
Acting Assistant Inspector General  
Financial Management and Reporting

Attachments:

As stated

## Report on Internal Control and Compliance with Laws and Regulations

### Internal Control

Management is responsible for implementing and maintaining effective internal control to include providing reasonable assurance that Army Working Capital Fund personnel accumulated, recorded, and reported accounting data properly; met the requirements of applicable laws and regulations; and safeguarded assets against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, the following material weaknesses exist that could adversely affect the Army Working Capital Fund financial reporting.

### *Previously Identified Material Weaknesses*

Management acknowledged that it is unable to comply with applicable reporting requirements and has identified the following material weaknesses, all of which are material, that continued to exist in the following areas.

#### **Financial Management Systems**

The Army Working Capital Fund systems do not meet the requirements for full accrual accounting. The systems do not collect and record financial information as required by U.S. GAAP. The financial and nonfinancial feeder systems do not contain the required system integration to provide a transaction-level audit trail for the amounts reported in the proprietary and budgetary general ledger accounts.

The Army continues to derive a portion of its financial information for the Army Working Capital Fund from budgetary transactions and data from nonfinancial feeder systems, such as the Commodity Command Standard System. The Army has implemented the Logistics Modernization Program system at all Army Materiel Command's activities except for TACOM Non-Army Managed Items and U.S. Army Medical Material Agency. These activities will continue to use the Commodity Command Standard System to report financial information until FY 2014 and FY 2013, respectively.

In DoD policy memorandum, "DoD Standard Chart of Accounts in Standard Financial Information Structure (SFIS)," August 13, 2007, the Deputy Chief Financial Officer directed the implementation of a DoD Standard Chart of Accounts in target general ledger systems. This memorandum also required that target system account values be internally crosswalked to the DoD Standard Chart of Accounts and transmitted using the standard format to the Defense Departmental Reporting System and other users of the data. The Logistics Modernization Program system is the Army Working Capital Fund's target general ledger system. However, the Army relied on crosswalks within Defense Departmental Reporting System to crosswalk Logistics Modernization Program system trial balance data to the DoD Standard Chart of Accounts format.

DoD Inspector General Report No. D-2012-087, "Logistics Modernization Program System Procure-to-Pay Process Did Not Correct Material Weaknesses," May 29, 2012, reported that the Army financial and system managers did not reengineer the Logistics Modernization Program system to perform Procure-to-Pay functions correctly or correct known material weaknesses. The Logistics Modernization Program system developers did not identify the system requirements needed to correct the root causes of material weaknesses, and Army managers did not review control activities to assess internal control effectiveness. As a result, Army managers continued the use of legacy business processes and the Logistics Modernization Program system failed to provide reliable financial data. This audit also identified data integrity issues associated with weak system access controls and the use of incorrect data attributes due to the lack of a single source for vendor data.

In December 2011, Increment 1 of the Logistics Modernization Program system entered into sustainment phase, and all new functionality for the system will be added as part of Increment 2. Increment 2 is in the planning stages and the implementation of this increment will continue through at least FY 2015, when the Logistics Modernization Program system will also transfer from a contractor-owned to a government-owned system. The Government Accountability Office, DoD Office of Inspector General, and U.S. Army Audit Agency continue to issue audit reports that identify significant data integrity and system integration problems, questioning whether the Logistics Modernization Program system will record transaction-level data correctly to support the financial statements. The Army does not expect to complete all corrective actions to resolve the financial management systems weakness until FY 2015.

**Inventory**

As of September 30, 2012, the Army reported 94 percent of its resale inventory in the Logistics Modernization Program system, which is capable of recording inventory using moving average cost. Consequently, the inventory valuation method used for 6 percent of the Army Working Capital Fund inventory does not produce an auditable approximation of historical cost as required by Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." The Army uses the latest acquisition cost method of valuing this inventory because the Army designed the Commodity Command Standard System for materiel management, rather than for accounting in conformance with U.S. GAAP.

Further, the Army reported that it did not properly baseline the transitioning of on-hand balances into the Logistics Modernization Program system using moving average cost. However, recent internal audit reports stated that the method used within the Logistics Modernization Program system to calculate the moving average cost was correct at the initial deployment site. Therefore, inventory valuations over time should have changed to comply with the Statement of Federal Financial Accounting Standards No. 3. However, further audit work is required to confirm this change. Additionally, since the majority of the sites were added during subsequent system deployments, the Army Working Capital Fund could not confirm the actual historical cost of this inventory and recognized that a significant portion may not be currently valued in compliance with Statement of Federal Financial Accounting Standards No. 3. The Army does not expect to complete all corrective actions to resolve this material weakness until FY 2015.

**General Property, Plant, and Equipment**

The reported value of Army Working Capital Fund General Property, Plant, and Equipment is unreliable because the Army lacks the documentation needed to support the historical acquisition costs of its assets. In addition, the Army has not fully implemented DoD policy that requires an entity to maintain information in its property systems on all property furnished to contractors due to system limitations. The Army is working with the Office of the Under Secretary of Defense (Comptroller) to develop a methodology to baseline acquisition costs for all property, plant, and equipment.

DoD Financial Management Regulation, volume 4, chapter 6, "Property, Plant, and Equipment," June 2009, requires the recording of the acquisition value of real property assets and associated depreciation on the financial statements of the DoD entity that funded the acquisition. Entities that use assets they did not fund must recognize their share of the assets' depreciation and sustainment and maintenance costs by either reimbursing the entity which records the asset on its financial statements or recording the imputed costs incurred on their financial statements. The Army has not yet taken actions to assess the assets reported in the Army Working Capital Fund real property accounts to determine whether the Army Working Capital Fund funded the assets reported on the financial statements. The Army expects to complete all corrective actions to resolve this material weakness in FY 2015.

**Accounts Payable**

Statement of Federal Financial Accounting Standards No. 1, "Accounting for Selected Assets and Liabilities," required intragovernmental transactions to be reported separately from amounts owed to the public and the establishment of an Account Payable upon acceptance of goods or services. The Army acknowledged that Army Working Capital Fund's systems do not track intragovernmental transactions by customer at the transaction level. As a result, the Army relies on unsupported adjustments processed by Defense Finance and Accounting Service personnel to report accounts payable balances. Additionally, DoD Inspector General Report No. D-2012-087 reaffirmed that the Logistics Modernization Program system could not generate an Account Payable upon acceptance of goods until they actually arrived at their final destination.

Additionally, Defense Finance and Accounting Service personnel adjusted Accounts Payable with the Public downward by \$149.0 million for undistributed disbursements. Army Working Capital Fund activities also could not reconcile their Accounts Payable transactions with the corresponding Intragovernmental Accounts Receivable that generated the payables. Therefore, Defense Finance and Accounting Service personnel made \$206.7 million in unsupported adjustments, which increased Intragovernmental Accounts Payable, forcing the amounts to agree with Army Working Capital Fund trading partners.

**Abnormal Account Balances**

In FY 2012, the Army Working Capital Fund Industrial Operations and Supply Management activities (limit-level) reported 19 abnormal account balances, valued at \$161.9 million. Army and Defense Finance and Accounting Service personnel used the 19 abnormal balances to compute the amounts reported on the Balance Sheet for such items as General Property, Plant, and Equipment; Inventory; Intragovernmental Accounts Payable; and Intragovernmental Other Assets. In addition, the posting accounts used to develop the proprietary trial balances in the Logistics Modernization Program system contained at least 542 abnormal account

balances valued at \$63.5 billion. The roll-up of limit-level account balances to produce amounts on the financial statements hid abnormal account balances in posting accounts.

#### **Statement of Net Cost**

The Army did not present the Army Working Capital Fund's Statement of Net Cost by major program, as required by OMB Circular No. A-136 (Revised). The Army Working Capital Fund's programs should align with the major goals and outputs described in the strategic and performance plans required by the Government Performance and Results Act of 1993. Army Working Capital Fund financial management systems did not accurately account for intragovernmental transactions or capture actual costs. Therefore, some of the information presented in the Army Working Capital Fund's Statement of Net Cost is based on non financial feeder systems. The Army plans to resolve this material weakness by FY 2015.

#### **Statement of Budgetary Resources**

OMB Circular No. A-136 (Revised) states that the entity should develop the Statement of Budgetary Resources predominantly from the budgetary general ledger accounts in accordance with budgetary accounting rules. The Army did not use data from the Army Working Capital Fund budgetary general ledger accounts reported by the Logistics Modernization Program system to populate the Statement of Budgetary Resources. Instead, Defense Finance and Accounting Service personnel continued to use budget execution data contained in status reports. In addition, Defense Finance and Accounting Service personnel made \$147.7 million in adjustments to the budgetary accounts because the accounting systems did not correctly record budgetary transactions related to Advances and Prepayments. The Army's target date to correct this material weakness is FY 2015.

#### **Intragovernmental Eliminations**

DoD was unable to collect, exchange, and reconcile buyer and seller intragovernmental transactions, resulting in adjustments that were not verifiable. DoD Inspector General Report No. D-2012-087 reported that the Logistics Modernization Program system did not capture the correct Standard Financial Information Structure business partner information at the transaction level needed to facilitate reconciling and eliminating intragovernmental transactions. DoD procedures require that the Army adjust its buyer-side transaction data to agree with seller-side transaction data from other Government entities, without the entities performing proper reconciliations. As a result, Defense Finance and Accounting Service personnel made \$724.1 million in adjustments to Army Working Capital Fund accounts to force the accounts to agree with the corresponding records of intragovernmental trading partners.

#### **Other Accounting Entries**

Defense Finance and Accounting Service personnel made additional unsupported accounting adjustments, valued at \$92.2 million, to force amounts to agree with other sources of information and records used in preparing the FY 2012 Army Working Capital Fund Financial Statements. The unsupported accounting adjustments represent a material uncertainty regarding the line item balances on the FY 2012 Army Working Capital Fund Financial Statements.

#### **Reconciliation of Net Cost of Operations to Budget**

Statement of Federal Financial Accounting Standards No. 7, "Accounting for Revenues and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting," requires a reconciliation of proprietary and budgetary information to assist users in understanding the relationship of the data. The Army could not reconcile the information reported in Note 21 with the Army Working Capital Fund's Statement of Net Cost without preparing \$557.1 million in unsupported adjustments to the general ledger accounts to force costs to match obligation information. To resolve this material weakness, the Army identified the implementation of tie point analysis capability within the Logistics Modernization Program system; however, the identified solution remained an unfunded requirement in FY 2012.

These financial management deficiencies may cause inaccurate management information. As a result, Army management decisions based in whole or in part on this information may be adversely affected. The Army reported that financial information may also contain misstatements resulting from these deficiencies.

#### **Compliance with Laws and Regulations**

Management is responsible for compliance with existing laws and regulations related to financial reporting. We limited our work to determining compliance with selected provisions of the applicable laws and regulations because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether

the Army was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on compliance with applicable laws and regulations.

### ***Federal Financial Management Improvement Act of 1996***

FFMIA requires DoD to establish and maintain financial management systems that comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. FFMIA also requires DoD to develop a remediation plan when its financial management systems do not comply with Federal financial management systems requirements. The remediation plan is to include remedies, resources required, and milestones. Army Audit Readiness personnel stated that the Army Working Capital Fund portion of the Army Financial Improvement Plan is currently under development.

For FY 2012, the Army did not fully comply with FFMIA. Army managers acknowledged that many of their critical financial management and feeder systems did not substantially comply with the Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2012.

### ***Antideficiency Act***

Section 1341, title 31, United States Code (31 U.S.C. § 1341) limits the Army and its agents to making or authorizing expenditures or obligations that do not exceed the available appropriations or funds. Additionally, the Army or its agents may not contract or obligate for the payment of money before an appropriation is made available for that contract or obligation unless otherwise authorized by law. According to 31 U.S.C. § 1351, if an officer or employee of an executive agency violates the Antideficiency Act, the head of the agency must report immediately to the President and Congress all relevant facts and a statement of actions taken. During FY 2012, the Army Working Capital Fund reported no potential or actual Antideficiency Act violations.

### **Audit Disclosures**

The Deputy Assistant Secretary of the Army (Financial Operations) acknowledged to us on March 30, 2012, that the Army financial management and feeder systems could not provide adequate evidence supporting various material amounts on the financial statements and that previously identified material weaknesses continued to exist. Therefore, we did not perform detailed testing related to previously identified material weaknesses. In addition, we did not perform audit work related to the following laws and regulations: Government Performance and Results Act, Prompt Payment Act, Provisions Governing Claims of the United States Government (including provisions of the Debt Collection Improvement Act), Federal Credit Reform Act, Improper Payments Information Act, and the Pay and Allowance System for Civilian Employees.

### **Recommendations**

This report does not include recommendations to correct the material weaknesses and instances of noncompliance with laws and regulations because previous audit reports contained recommendations for corrective actions or because audit projects currently in process will include appropriate recommendations.



## Department of the Army Comments



REPLY TO  
ATTENTION OF

**DEPARTMENT OF THE ARMY**  
OFFICE OF THE ASSISTANT SECRETARY OF THE ARMY  
FINANCIAL MANAGEMENT AND COMPTROLLER  
109 ARMY PENTAGON  
WASHINGTON DC 20310-0109

7 November 2012

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDITING,  
DEPARTMENT OF DEFENSE

SUBJECT: Management Response to the Fiscal Year 2012 Army Working Capital Fund  
Financial Statement Audit Report

1. Please accept our thanks the Office of Inspector General for your efforts on behalf of Army and the professionalism exhibited by your staff during the audit. We appreciate the opportunity to comment on the draft reports provided to us on November 5, 2012.
2. We generally concur with the findings identified in the draft Report on Internal Control. We will prepare corrective action plans to address the identified findings as part of our audit readiness effort. Our audit readiness contractor will begin examination of the inventory line item for existence and completeness (E&C) in the near future. During the upcoming year, they will continue work on developing a complete Army Working Capital Fund Financial Improvement Plan with obtainable milestones that encompasses the remaining open OSD 23 issues and the procure-to-pay plan of actions and milestones.
3. With Standard Financial Information Structure implementation and improved Army Enterprise Systems Integration Program governance, we anticipate obtaining waivers for our intragovernmental eliminations material weakness in Fiscal Year 2014. Intragovernmental transactions will include specific Federal trading partner codes. This will enable reconciliation of intragovernmental transactions between Federal agencies, elimination of intragovernmental transactions in the financial statements, and supportable quarterly reporting to Treasury and OMB of US Standard General Ledger account balances related to transactions with other Federal agencies.
4. My point of contact for this action is [REDACTED] [REDACTED] can be reached by telephone at [REDACTED] [REDACTED], or by e-mail at [REDACTED]

A handwritten signature in black ink, appearing to read "James J. Watkins", is positioned above the printed name.

James J. Watkins  
Deputy Assistant Secretary Army  
(Financial Operations)

We are interested in your feedback regarding the content of this report.  
Please feel free to e-mail your comments to AAFS@hqda.army.mil or write to:

## **Department of the Army**

Office of the Deputy Assistant Secretary of the Army  
(Financial Management and Comptroller)

Office of the Financial Reporting Directorate  
Room 3A312, 109 Army Pentagon  
Washington, DC 20310-0109

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## THE SOLDIER'S CREED

I am an American Soldier.  
I am a Warrior and a member of a team.  
I serve the people of the United States  
and live the Army Values.

I will always place the mission first.  
I will never accept defeat.  
I will never quit.  
I will never leave a fallen comrade.

I am disciplined, physically and mentally tough,  
trained and proficient in my warrior tasks and  
drills. I always maintain my arms,  
my equipment and myself.

I am an expert and I am a professional.

I stand ready to deploy, engage, and  
destroy the enemies of the United States  
of America in close combat.

I am a guardian of freedom and the  
American way of life.

I am an American Soldier.